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ROYAL COMMISSION ON TAXATION

Proceedings of hearings held before the Royal Commission on Taxation in the Supreme Court of Canada Building, Ottawa, Ontario, commencing at 9;30 a.m. on Saturday, January 18th, 1964.

COMMISSION:

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RESEARCH DIRECTOR

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SECRETARY

MR. G. L. BENNETT

INDEX TO EXHIBITS

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SUBMISSION OF THE EXECUTIVE COUNCIL OF THE CANADIAN CHAMBER OF COMMERCE.

APPEARANCES: Mr.G.E. Brown
Mr. C. Leach
Mr. D.L. Morrell
Mr. A.J. Little
Mr. G. Keeping
Mr. L. Kent
Dr. J.R. Petrie
Mr. W.J. McNally
Mr. E. Hamilton

THE CHAIRMAN: Mr. Secretary, I think we can start.

THE SECRETARY: Good morning, Mr. Chairman and Commissioners. Today we have a submission by the Canadian Chamber of Commerce. Mr. G. Egerton Brown, President of the Executive Council of the Chamber, is here with a delegation. He wishes to make a few opening remarks and introduce some of his colleagues.

I would like to enter this brief into the record as Exhibit 325.

--- EXHIBIT NO. 325: Brief of the Executive Council of the Canadian Chamber of Commerce.

THE CHAIRMAN: Thank you, Mr. Secretary.

Good morning, Mr. Brown and gentlemen. It is nice to have the Chamber back with us again. You were helpful when we started and put us on the track. We hope we have followed the track that you put us on. We have gone a long way, I might say, since then. You provide us with an extremely interesting document. I might say that when I commenced on it last night it looked very formidable, and it was very formidable; but it is extremely well written, with an easy pen, and to my way of thinking, quite a joy to read. I thoroughly appreciated it.

We will certainly have questions to ask of you, but before we do that I would be very glad to hear anything that you would care to say to us.

MR. BROWN: Thank you, very much, Mr. Chairman. Mr. Chairman and Members of the Royal Commission on Taxation; this is Saturday morning, and we do appreciate and thank you for your courtesy in meeting with us on this occasion. It is unfortunate that illness and other untoward events prevented us from keeping our appointment with you last November 25, and I say again, thank you for your courtesy in providing this opportunity to meet with you.

The Executive Council of the Canadian Chamber does welcome this opportunity of appearing before this Commission for a second time. We have followed with very considerable interest your hearings as they have been reported in the press and as we have heard of them from those who have

participated in them. We would like to take this opportunity to commend you, sir, and your colleagues for the obviously thorough job you are doing in fulfilling the Commission which you have been given by government. We should like to report that the appointment of this Commission fulfills a request that the Chamber made to government for a thorough review of the Canadian tax structure, and we are grateful that this exhaustive survey is in such competent hands.

As you know, the Canadian Chamber of Commerce is the national voluntary federation of more than 8000,00 autonomous Boards of Trade and Chambers of Commerce -- those terms are synonymous -- across Canada. These Boards or Chambers vary in size from the very large Boards of Metropolitan Toronto, Vancouver and Winnipeg, the twin Boards of the Chambre de Commerce de Montreal and the Montreal Board of Trade, down to those in the small communities scattered across the face of Canada. In fact, 75 per cent of these member Boards come from towns of less than 5,000 population.

In total, over 125,000 business and professional men and community leaders make up the membership of these member Boards of the Canadian Chamber. These organization members -- that is, these Local Boards of Trade and Chambers of Commerce -- are the voting members of the Canadian Chamber of Commerce. They are the ones that determine the policy of the Chamber. Each of those Boards has one

vote, and only one vote. So that it is completely democratic in that respect.

In addition to these organization members there are non-voting members of some 2,700 corporations and some 25 associations.

Again, to make it clear, sir, I would like to indicate that the organization of the Canadian Chamber consists of national officers and a National Board of Directors. This national Board meets at the time of the annual meeting of the Canadian Chamber and once or twice at other times during the course of the year. During the interim periods between meetings of the Board, the Executive Council carries on the ordinary business of the Chamber.

As your Secretary said, I am Egerton Brown, the Chairman of that Executive Council. The policy of the Chamber originates with standing committees of the National Chamber, or with the individual Chambers or Boards across the country and their standing committees. Proposed policy is clarified and refined by action of standing committees of the National Chamber and referred back to all the individual Chambers across the country for their comments and concurrence. It then goes through the process of the National policy Committee at the annual convention, and finally through the plenary session of the annaul convention of the Canadian Chamber and comes out in the form of a policy statement for the Chamber.

The men who carry on this work in the Chamber come from all across Canada. They are engaged in the natural resource industries of agriculture, fishing, mining, lumbering and so forth. They are engaged in manufacturing, primary and secondary. They are engaged in trade and distribution, foreign and domestic, wholesale and retail. They are engaged in communications, in transportation. They are engaged in public utilities. They are engaged in finance, insurance, banking, investments and so forth. They are also in the related professions of accountancy, law, architecture, engineering, and so on.

Their work comprises the warp and woof of the Canadian economy. I mention this to underline the fact that we come before you, sir, and your colleagues not to plead a special case, but to speak for that vital element of the Canadian economy which supplies the employment and finds the money for the payrolls of the country.

Mr. Campbell Leach has served as Chairman of a special committee that prepared the Executive Council's submission, and he and his committee are here today.

I should now like to introduce Mr. Leach to you, sir, and to your associates on the Commission and to the staff of your Commission. Mr. Leach is well known to you, sir, and I think to your associates. He has brought to his task a deep understanding of the problems which our Canadian

tax structure creates for Canada. Before asking Mr. Leach to carry on I would like to introduce Mr. D. R. Morrell, General Manager of the Canadian Chamber of Commerce. Don is at the extreme left.

Mr. Leach will now, I think, introduce the other members of the delegation and will make an opening statement on the submission you have received in advance of this hearing. He will also act as the leader in any discussion you may wish to carry on in respect of that submission. Mr. Campbell Leach.

THE CHAIRMAN: Thank you, Mr. Egerton Brown. Before Mr. Leach commences, I would just like to acknowledge the very kind remarks that you made about ourselves. Thank you, sir.

We are aware of the great significance of the Chamber and its role in the Canadian community, and very clearly what is said to us today is of great importance to us in our deliberations in this task. I do not now know how we could undertake such a task without knowing the views of the Canadian Chamber. Yes, Mr. Leach.

MR. LEACH: Mr. Chairman, I would first of all like to associate myself with the words of appreciation that have been expressed by Mr. Brown, particularly in reference to your kindness in sitting on Saturday. I myself always work on Saturday, but I realize that perhaps some of the Commission or some of the people here may like to have the weekend free.

The brief which we have filed with you is the brief of the Executive Council of the Canadian Chamber of Commerce, as Mr. Brown has explained, and it has been prepared to conform with the policy of the Chamber as expressed in its annual policy declarations.

We believe that the Chamber is qualified to speak for Canadian business, but a great effort has been made to arrive at our conclusions in an impartial way. We have refrained from making recommendations designed to favour business at the expense of other segments of the community. Thus, our recommendations express what we believe to be in the best interests of Canada and its economy. In short, what is good for the country is good for General Motors.

You will have seen that we have not dealt with those matters which are often referred to as "inequeties, loopholes and anomalies" in the taxing statutes because many of these have been dealt with in our annual submission to the Ministers of Finance and National Revenue, copies of which we have filed with you, and because we believe that these have been adequately dealt with by other submissions; thus we prefer to view the problem from higher ground and to avoid entanglement in the underbrush.

We strongly urge that the Canadian tax-climate should be such as to be at least as attractive to production and investment as any in the world. This means that taxes on business income,

A-8

investment income and personal income should be lower. Lately it has been popular to discourage foreign investments but it should remembered that British capital originally, and United States capital latterly, have been vital to us. Consequently, while it may be desirable to encourage Canadian investment at one time and foreign investment at another, the fact remains that the development and growth of a country depend upon investments.

Conversely, we suggest that the necessary revenues to replace the loss from the reductions of rates applicable to business and personal incomes should properly come from consumption taxes of one form or another. One of the classic bases for taxes is upon consumption or enjoyment. As a nation, are we not living beyond our means? Wages, salaries and fringe benefits are higher than ever before. The dollars spent from these sources should be taxed on a broader base.

Thus, we should stimulate effort, initiative, savings and investment on the one hand, and tax the personal enjoyment of mass income on the other. Consequently, our thesis is a broader tax base and lower income tax rates.

Equally important is the tax atmosphere. Policies should be stable, consistent and reliable. Integrity should be a characteristic of fiscal policy and certainly a characteristic of tax law. Abrupt, unpredictable, illogical, or crisis-inspired changes should be avoided; retroactive or discriminatory

taxes should be shunned. Investment capital is sensitive to these, and business places political stability thighe on the lists of requirements. This is particularly true of foreign capital which views with alarm our succession of financial crises and reacts accordingly.

I realize that much of what I have just said has also been said by earlier submissions to this Commission and in other public pronouncements, but I would strongly deny any accusation of plagiarism because we arrived at this point of view more than a year ago, and this is something about which we feel very strongly.

Mr. Chairman, I will now introduce to you the members of our delegation who have not already been identified to you. I am sure that you will wish to direct questions to us. We have allocated the subject matter in a broad way, but naturally we are all available for any questions which you would like to ask on any particular subject.

At my extreme right, Mr. George Keeping, the former Chairman of the Executive Council preceding Mr. Egerton Brown. Then, Mr. W.J. McNally, who is the manager of the Policy Department of the Canadian Chamber of Commerce. Then we have Dr. J.R. Petrie, who I am sure is known to you, Mr. Chairman, and he may even be known to other members of the Commission. Perhaps Mr. Perry may be acquainted with him. Dr. Petrie is primarily responsible for the drafting of our brief, and especially for the economic analysis

upon which it is based.

On Mr. Brown's left is Mr. A.J. Little, the First National Vice-President of the Chamber of Commerce; that is to say, on its Board of Directors, the senior Board. Then we have Mr. Eric Hamilton. Then there is Mr. Lionel Kent and, of course, Mr. Morrell has already been identified to you.

I think that is all I have to say, Mr. Chairman, and we are in your hands.

THE CHAIRMAN: Thank you very much, Mr. Leach. This morning it seemed to us, in view of the size and the weight of this tome and its contents, technical aspects and so on, that we might do well to use our counsel, Mr. Coyne, in leading our questions. So I have asked Mr. Coyne to undertake this task. I think that without further ado, Mr. Coyne, you might proceed.

MR. COYNE: Thank you, Mr. Chairman. Mr. Leach, I wonder if we might start out in a general sort of way by taking up what I might call the general theme of your brief, namely your concern that on both the expenditure and the revenue side in recent years there has been too much emphasis on the stimuls being given to consumption and a lack of emphasis on the problems of investment and capital expansion.

On page 2, for example, in paragraph 7 you say:

> "If government expenditures are permitted to continue to rise at the pace of recent years a disproportionate share of the

national product will be siphoned off into government channels to the detriment of the private sector. In particular we are concerned that an ever-increasing share of government expenditure is being directed to the support of consumption at the expense of capital accumulation and investment. If the Canadian economy is to maintain a satisfactory rate of growth there must be more emphasis on increased savings, capital investment and productivity, and less on new welfare programs."

Then over on page 4, taking the revenue side of the picture you say in paragraph 12:

"However, just as recent programs of expenditure have tended to concentrate too heavily on the support of consumption, so in our view the present tax structure has tended to sap the vigorous spirit of enterprise and initiative on which the nation must rely for continued expansion. A necessary and desirable reform would be to reduce the present reliance on personal and corporate income taxes, and restore the incentive to venture and invest in an expanding Canadian economy".

Going on in paragraph 13, you state:

"It is desirable that attention be given to some shift in emphasis from taxes on income to taxes on expenditure so as to

-12

encourage industrial expansion and employment and stimulate private initiative and effort."

It probably will not be surprising to you that some bodies which have come before the Commission and which have similarly examined the record, if you like, of the last ten years have come to quite a different conclusion. For example, they have directed our attention to the great investment boom of 1955 to 1957. They have stated that during that period tax rates were relatively the same; that is, tax rates on income of various kinds were relatively the same as they are today; that at that time of time the tax structure did not seem to inhibit capital expansion; and further, to them what was the key, or the touchstone, if you like, was the great upsurge of demand both present and anticipated, and that in the presence of such a demand situation business had no problems in finding the necessary capital to expand its plant in order to satisfy this demand. Finally, if I interpret their position properly, they attribute the doldrums, if you like, of the last few years as being attributable, not totheeffect of the tax structure on capital investment but to the falling off of demand for the products which manufacturers produce.

I wonder if you would care to comment on that point of view, in relation to the somewhat different view which you take here.

MR. LEACH: Mr. Chairman and members of the Commission, I think I could give a layman's

-13

answer to that question, but this is in the nature of economics and economic analysis, and I think I will ask Dr. Petrie to answer that question.

MR. COYNE: You and I are both laymen in this field, Mr. Leach.

DR. PETRIE: Mr. Chairman, Mr. Coyne, you raised the point of the expansion of the capital program. If anybody in Canada has said that our tax structure has not deterred the capital expansion program, I think they forget that this capital expansion program has been largely the result of foreign investment in Canada.

We have been financing this great expansion, this boom, by borrowing from abroad; borrowing, as well as direct investment from abroad, from American corporations in direct investment in Canadian subsidiaries. Up until recently there has been no disincentive in our tax system to this capital expansion through foreign funds. Currently I think -- this is my personal view; I am not speaking for the Chamber -- there has been, because of this withholding tax situation, probably an area of confusion.

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Supposing, for the sake of argument, Mr. Chairman, we had tried to support our own expansion programme with savings and investments, it couldn't possibly have been done, because that was all accrued income, or personal income. We certainly couldn't have supported the rate of capital expansion going on in the country.

Nevertheless, if we had the tax climate which the Chamber is advocating there would have been more capital available, in our view, for Canadian expansion and less dependence on foreign investment; but, nevertheless, we never could have supported the rate of capital expansion.

So my answer is that, as an economist, I still feel that the weight of taxation on the savings and investment segment of the economy has distorted the pattern of our development. But even although we had had what we are advocating before you we still couldn't have supported the rate of growth of the economy.

THE CHAIRMAN: If I may interrupt, didn't I hear Dr. Capon referring to the revenue of the country's growth resources, and he indicated the accumulation of earnings which, from his figures, indicated about 80 million dollars a year...

DR. PETRIE: Yes.

THE CHAIRMAN: I think it is now about 3 billion dollars a year, and with that and equity issues of 350 million and bond issues of 400 million it seems to me that this is by far the largest

source of earnings. I suppose the answer is that even that isn't enough, but it seems to me that...

DR. PETRIE: On your figures, and doing a little mental arithmetic, it is about $4 billion; and total expenses would be $9 billion.

MR. COYNE: That includes Government spending?

DR. PETRIE: Yes; $9 billion, roughly. But the business segment of that is what? It is difficult to project because we haven't got our anticipated figures for 1964.

THE CHAIRMAN: We had the Construction Association and they said 7, 6 for total expenditure and that something over 2 would be housing; quite a large part Government and business; and I would have thought nothing like 7, 6.

DR. PETRIE: Supposing it were 6 or 7 billion. We couldn't still, even with this -- we couldn't begin to generate the amount necessary to support the economy; and all we are saying is that the present tax structure is curbing our ability to support ourselves; and even although we could get all we wanted from the Government we still can't support ourselves.

THE CHAIRMAN: Thank you.

MR. LITTLE: With the greatest respect, and on the submissions that have gone before, I, as a layman, would like to take up the point that it is the variation in the demand side that causes the fluctuation in our economy rather than the availability.

It seems to me that we are outside the economic pattern. Surely each of us must realize that this is not realistic. There is no lack of demand, really, for material. If it were true that there was a holdback on the consumption side then you would expect that; and that it would be even true on the savings side; and this is not borne out by the facts which have been submitted; and I think that this is true of personal income, too, that so far as personal savings are concerned, going back for a number of years there has been a gradual decline in personal savings accumulated.

This, it seems to me, is the real answer.

THE CHAIRMAN: Personal saving, has set out in your exhibit 11, is going up at quite a good rate. In 1957 it was 1,202, in 1961, 1,509, and in 1962 a great leap up to 2,331.

MR. LITTLE: At the same time the dollar was changing in value and the number of people was going up. This must be related to it.

In the period 1926 to 1930 the proportion of gross savings to income was 22.7%; in 1946 it was 7.2% and in 1962 it was 5.9%.

MR. COYNE: I think that this appendix is a very interesting document. I was proposing that we might return to it later.

MR. BROWN: I think, Mr. Chairman, there is the fact that the 10-year period which you suggested originally in your first comment is not

sufficiently long to give us a really clear picture.

If we think only of the post-war period we are thinking of times when the world situation in trade favoured Canada, but with the resurgence in Western Europe we have a quite different situation today. This, I think, has a bearing on the demand side, and it also has its bearing on the need for our being able to borrow our own capital.

If you go back and look at appendix 3 you will see in that what has happened in relation to direct and indirect taxes over a period of years, and how at one time direct taxes were a very much smaller portion of the total in the federal picture.

COMMISSIONER PERRY: The way your argument has developed, it is on the basis that the idea is to keep a balance between consumption and investment.

MR. BROWN: That is right.

COMMISSIONER PERRY: I do think that business people tend to be carried away a little by the investment side. On the other hand, business people don't invest simply for the purpose of building factories; they invest to meet a market demand.

MR. BROWN: And that is the thing which is dynamic in the Canadian picture; this is the thing which creates continued business.

COMMISSIONER PERRY: It is not going to be dynamic if there is no market demand.

MR. BROWN: If the market can be forced and can be met through...

COMMISSONER PERRY: I would go so far as to say that the great thing about the free enterprise system is that if there is a demand there is no force on earth that can keep free enterprise from beating that demand -- not even taxes.

MR. LITTLE: If there is no market there is no demand.

THE CHAIRMAN: The Americans, when they came to have taxes of 11 billion dollars, tried a system of stimulation of demand and stimulation of investment, but they have now worked out a proportion between the two because there was no benefit of one without the other.

COMMISSIONER PERRY: I think the important thing is that you don't invest for the sake of investing. There is no point in investing your money when there is no consumption.

MR. KEEPING: It is a question of balance, and in our view it has become out of balance and it needs to be put back in balance again.

COMMISSIONER PERRY: I gather this is in your brief, and it occurs quite frequently.

MR. COYNE: Turning over several pages, and still dealing with the general, introductory part of your brief, you refer on page 9 to tax pyramiding which, you say, represents one of the major distortions in the tax system; and then you say:

> "The spread between the statutory and effective rate of sales tax is sometimes almost fantastic. Thus, the effective rate on

Canadian cigarettes of federal sales and excise taxes is 209% of the manufacturers' selling price net of taxes..."

This is rather a small point, but I put it to you that all that is derived from this final sentence is that Governments in their wisdom have decided that the effective rate of tax on Canadian cigarettes shall be 209%; and it doesn't much matter. They have decided, in their wisdom, to impose this tax in a series of somewhat obscure and perhaps hidden forms, but if they had not done that they would have imposed a tax of 209% on the retail price of cigarettes; and what would the difference be? What is the significance which you have to draw from this examination of tax pyramiding?

MR. CHUTTER: Well, I think the point we are making is that through this particular pyramiding operation you have concealed taxes which are not known to the public. The point is that should the Government of the day impose that kind of levy I think there probably would be political outcry; but because practically no consumer knows what he is paying there isn't much of an outcry.

The same thing applies on liquor, for instance. The effective rate of sales tax on spirits is about 33% instead of 11%, but nobody seems to know that, so there is no outcry.

Really all we are trying to do is to point out that through the pyramiding of these taxes you have the situation that we have tried to point out, that the spread between the statutory and effective rate

of sales tax is really fantastic; and yet hardly anybody appearing before this Royal Commission has taken the trouble to analyze the situation and point it out.

MR. COYNE: Would the tax structure be improved if hidden taxes -- which, I think, is the popular phrase to describe this situation -- were abandoned?

MR. CHUTTER: Well, I wouldn't say we could abandon the hidden tax, but I do think that the taxpayer should know what he is paying.

THE CHAIRMAN: Somebody told us they didn't believe that the housewife knew there was an 11% manufacturers' tax and he was perfectly sure that they had no appreciation of the impact of it on themselves.

MR. CHUTTER: I think that is probably correct.

I would like to see the Canadian public -- the taxpaying public -- becoming fully aware of the taxes that are being paid. This is my personal view; because most of us are not sophisticated enough to know what taxes we do pay. We know about our income tax, but we don't know about things like provincial sales tax which is changed at the quarter.

COMMISSIONER PERRY: May I inquire along the lines of whether you are trying to keep the taxpayer content...

MR.CHUTTER: Mr. Perry, I would like the taxpayer to know exactly and then maybe he would

take some action at the polls to keep down Government expenditure.

MR. LITTLE: It seems to me that through all this dicussion we seem to assume that the taxpayers are different from the Government, and that there are two sides here. It seems to me that the answer becomes very clear when we straighten out our thinking and realize that the Government is here to serve the people and not vice versa; and I can't see any other proper answer but that people ought to know what they are paying for the services that they receive.

It seems to me that it is quite wrong to suggest that there is some moral reason for disguising what the people are being asked to assume in the way of a tax burden.

THE CHAIRMAN: The point really is, Mr. Little, whether, if one is levying a tax at some level other than the consumer's level, any good purpose would be served in showing people what that tax may be on the goods they bought.

Now, this assumes that it is a good thing to have it at that level, and, secondly, to show where the taxes are. If you are recommending a change in that level that is something else, but I don't think you are. You are saying it is not a good idea to conceal taxes.

COMMISSIONER WALLS: I think, with the complexity of the different types of taxes, the only way you could do this would be in the explanatory notes for budget speaches, where you could show in a concise

way what the overall tax burden is; and then you could find the tax expenditure by taking one tax at a time. In this way their overall tax burden could be given to them once a year.

COMMISSIONER PERRY: The tax foundation issues a publication on this. I would think that the taxpayer is fairly intelligent and he could pretty well work out what his total tax burden was within a relatively small percentage; but I doubt if the Tax Foundation has been inundated with orders for this publication.

MR. CHUTTER: This is the problem.

MR. LITTLE: It seems to me that this just provides the answer. Surely it is ridiculous that the people of the country have to hire an agency to find out what taxes are being imposed upon them. Surely this is ridiculous. Surely it is right that they should know. You will quite appreciate that we are not suggesting that every tax must be laid on the table; but from the tone of Mr. Perry's question I thought that perhaps he was implying that it was right and proper that the people ought not to know.

COMMISSIONER PERRY: If I left that impression I certainly hasten to withdraw it. I am merely interested in the mathematics of this operation. It may not require an agency to tell them, but it certainly would require an agency to work out the arithmetic.

THE CHAIRMAN: We have had a lot of people who have stated that the taxes should be seen

by every person so that they would know what it was when it was paid. The question is what kind of redesigning of the system is necessary in order to achieve this thing; and certainly on that basis most of our present taxes would disappear and something else would have to be done, I think.

. 18

Most people tell us that it is the corporation tax and they deduct it against the individual. In that case you have to throw corporation taxes out and find something else. You have to be able to identify the individual, I suppose. But I do not think you are suggesting that we throw everything out and that the individual cannot see how the tax should bear on him.

COMMISSIONER PERRY: I think we are all for enlightenment.

MR. COYNE: I wonder if we could now turn to page 14.

COMMISSIONER PERRY: Might I just raise one question first of all. At the bottom of page 9 you begin using what is a fairly standard comparison, and that is taxation as a percentage of national income. I do not disagree that this is one basis of comparison, but I do not think that it is the one most commonly used. The one more commonly used is the gross national product, but I think there are good grounds for using the gross national product. Would Dr. Petrie have anything to say as to why he adopted this method rather than that of the g.n.p?

THE CHAIRMAN: He used the g.n.p. one.

DR. PETRIE: Yes. We used it both ways actually, but I felt the percentage figures of national income were more impressive, really more frightening, than the g.n.p.

COMMISSIONER PERRY: You and I can have a discussion about this afterwards, but I do not think you are really comparing like with like, because, as

-2

you know, gross national product includes the indirect taxes which are in your tax comparison.

MR. PETRIE: That is right.

COMMISSIONER PERRY: I think you are comparing more like with like.

DR. PETRIE: On the otherhhand,Mr. Perry, if you take national income, this is the doh-ray-me in the hands of people. I like to think, speaking strictly from a personal point of view,that I have an income of "x" dollars. That is my portion of the national income and the tax bite is so much, let us say 40 per cent or "x" per cent. To me it is more realistic than measuring the market value of goods and services which are produced by the nation.

COMMISSIONER PERRY: I agree, but normally when comparing or determining part of the whole you are looking at the whole which includes that part.

DR. PETRIE: But if we are taking national income we are taking something with a dollar value which is the income of the nation. Then we compute how much of that is taken away by taxes, and it comes -- I think the figure I have used is 42.6 per cent in 1961.

COMMISSIONER PERRY: Yes, it is a valid comparison.

DR. PETRIE: I cannot quarrel with you about this because I used it in both ways.

MR. BROWN: At the top of page 11 it is shown both ways.

COMMISSIONER PERRY: Actually, our staff

statistician introduces so many other factors that we really do not know what the proper comparison is.

COMMISSIONER WALLS: I was also wondering about paragraph 22, where you are dealing with revenue and expenditure trends. On the next page, table I, true you are relating that to the tax burden, but do you not think that it would have been fairer to show the relationship of the total revenue of the government rather than those taxes, because your additional revenue is about 20 per cent more than the tax revenue, and the relationship then between revenue and expenditure is much closer together.

DR. PETRIE: I am sorry, I did not get your paragraph reference there.

COMMISSIONER WALLS: Page 9, where you are dealing, first of all, with revenue and expenditure trends. True, on page 10 there is the heading "Weight of the Tax Burden", and I agree that we are discussing taxes here. But generally speaking you are bringing out the increasing spread between revenue and expenditure. If you are doing that, is it not fair to show the relationship between total revenue as well as taxes, because that amounts to 20 per cent of the tax take. If you add that to it, the relationship between revenue and expenditure is not merely as extreme as you attempt to make out it is.

DR. PETRIE: Again, it is a problem of semantics, Mr. Walls. I do not think that you could get six statisticians together and get six unanimous views. All we have done is to take our examples and

point them out to you. I am quite flexible about all these figures. I will discuss them on any ground at all. But I think that what we have done here points up a trend. That is all we are trying to do.

THE CHAIRMAN: I want to deal with the trend on page 11. Are you moving on beyond page 11, Mr. Coyne?

MR. COYNE: Yes, Mr. Chairman. Perhaps you would like to take it up there.

THE CHAIRMAN: I can remember the 25 per cent limit, which is suggested in paragraph 26, in the year 1945. I suppose that it is a very good thing that we pay no attention at that time, because it seems to me that as taxes have gone up so has prosperity. I suppose the key to that is that our disposable income, if taxes kept on rising, and in fact I think it must keep on rising from year to year, because your figures show that. Indeed, we see more evidence of good living in the form of new automobiles, increased sales, better homes, more refrigerators. We are living in a time of prosperity as far as I can see.

At the same time, our taxes keep on getting steeper and we keep on complaining more about them, which is very natural, and I am not surprised that we should.

But, Dr. Petrie, is there a lesson in this? Had we been sitting around in 1945 as we are now, we would all have been saying that we must not go beyond 25 per cent, and we would all have been wrong.

DR. PETRIE: That is right. Now I am confused, as I suppose all economists must be, Mr. Chairman. Some of us heeded the warning of 25 per cent. Some of us did not. Obviously the government did not. We have an affluent society today despite the all time record tax burden. We still have more net disposable personal income that we ever had before.

Personally, I have spent a good many hours thinking: Is there a point beyond which there is no return? There must be somewhere. I am not prepared to say where it is, sir, but I am getting suspicious that we are coming close to it, if I may say that.

From the point of view of personal incentive, Mr. Perry and I have argued at great length over the years about incentive and disincentive vis-a-vis taxation. But there comes a point at some place in time where you do get beyond the point of no return, but I am not prepared to say where that point is. Is it 25 per cent? That is stupid. Thirty per cent? Well, we have gone beyond that. Is it 35 or 40 per cent? Where it is, I do not know. But there must be a point somewhere where your tax burden becomes inflationary. This is the only general principle to which I will subscribe at the moment.

THE CHAIRMAN: I thought that tax burdens were deflationary.

DR. PETRIE: No, I think they would be inflationary in the longer run.

THE CHAIRMAN: I know one country which

cannot reduce its taxes, because if it did it would be faced with inflation. That is the short-run, I suppose.

DR. PETRIE: Yes, the short run.

MR. LITTLE: Mr. Chairman, I would not like to leave on the public record, and certainly in the minds of the press, any implication from your question that the Chamber of Commerce would agree that there was a necessary relationship between high taxes and the prosperity which we enjoy.

THE CHAIRMAN: Well, that is the point I was making all right.

MR. LITTLE: It is true that taxes have been high and have continued to grow, but this is like saying that there are "x" million more people dying in Canada today and we are also more prosperous. I do not think there is any relationship between the two at all.

At the same time, when one says that we have proved that 25 per cent is wrong, how one can take that stand firmly without knowing what the situation might have been had we not gone beyond 25 per cent. I do not know. We might have been far more prosperous and had a far greater expansion of the economy if we had not had such a high rate of tax. What I am trying to say is that because there had not been a denial of what you have put to us, it does not mean that this is something which we will accept.

THE CHAIRMAN: Well, I think the record is clear on that now.

-7

COMMISSIONER PERRY: In this connection let me just tell a story which perhaps the reporter had better not take down.

--- OFF THE RECORD.

DR. PETRIE: Well, I think the point has been made by Mr. Little that we do not know what would have happened had we had a tax burden of only 25 per cent. We might have been more or less prosperous than we are now.

MR. COYNE: Could we now turn to page 14 for the moment, where you are speaking of the changing pattern of the tax mix in paragraph 33, and you make reference to Appendix III. Then you say:

> "The heavy concentration on income taxes began during World War II, and since then it has continued on an increasing scale, as shown in Table II."

Then Table II does substantiate your statement, of course.

If you would now turn to Appendix III, you have, of course, for reasons of space, only chosen particular years, approximately every fifth year. We have seen figures for each year over the last ten years, from say 1954 to 1963, or from 1953 to 1962. Those figures deal with the same question. My recollection is that those figures indicate that over that period, certainly over the period of the last seven or eight years, the proportion of federal

taxation represented by the direct taxes you are speaking about has really remained quite constant at about 60 per cent. The portion made up of the federal sales tax has actually over the period increased slightly from 18 per cent to 19 per cent, I think, although I am speaking from recollection because I do not have the figures before me.

I am wondering whether there is any disagreement here from this general statement, or whether you are speaking of a longer term trend.

DR. PETRIE: This is a long-term trend of direct versus indirect.

MR. COYNE: Do you agree with me that, say, from 1954 onwards there has been relatively little change in the division?

MR. PETRIE: Yes, I would agree with that. It has been relatively stable in the last four or five years, but we went back to the 1920's, when the direct taxes were only 15.7 per cent of the total.

MR. COYNE: What made me query it, Dr. Petrie, is the fact that in this sentence you speak of the "heavy concentration on income taxes which began during World War II, and since then have continued on an increasing scale."

MR. PETRIE: It has to some extent. Here again, we get into the lovely problem of semantics, and the question what is direct taxes and what is indirect taxes. In accordance with Section 92 I said that provincial taxes according to the constitution are direct, and I have thrown them out.

-9

MR. COYNE: I want to pick that up in a moment, but here I think we are talking of the federal field only, where the distinction is relatively clear.

DR. PETRIE: Yes. In the last few years I agree with you that the proportion has been stabilized.

COMMISSIONER WALLS: In the federal figures you have included customs tariff. Do you think that that is fair in giving an illustration between direct and indirect taxes? Because your customs tariff has no relationship to revenue requirements whatsoever --

COMMISSIONER PERRY: Wait a moment!'

COMMISSIONER WALLS: Just let me finish -- in that its changes are not geared to revenue at all. At the present time our negotiators are leading discussions under the sponsorship of GATT on the Kennedy recommendation in connection with the European common market. Next year we will probably encounter a considerable cutting of customs tariffs, which have no relationship to the revenue requirement of the government. That is why I am wondering, when considering direct and indirect taxes, whether the customs tariff should be kept out as a distinct unit.

DR. PETRIE: How do you exclude customs duty in differentiating, say, between excise duties? It is the same sort of thing.

COMMISSIONER WALLS: Yes. Your excise duty is a corresponding tariff on two main items to the customs tariff. That is quite right.

THE CHAIRMAN: Are they not revenue measures?

COMMISSIONER WALLS: Yes, they are. But it is questionable whether your customs tariff today is principally a revenue measure or a protective measure.

DR. PETRIE: Well, I am not able to speak for the government on that, but personally I have always felt that the customs revenue was a pretty vital item in the national budget.

COMMISSIONER WALLS: Yes, it certainly is. But when considering the relationship between direct and indirect taxes, would it not give a clearer picture if it were left out?

DR. PETRIE: I would not think so.

COMMISSIONER PERRY: In 1929 it was nearly all of the federal revenue. The other taxes have nearly all been repealed.

COMMISSIONER WALLS: Yes, but we are in a different year from 1929 now.

MR. COYNE: Turning the page and picking up your division of direct and indirect taxes -- and I think this question is really a matter of semantics -- you point out in paragraph 35 on page 15:

> "In accordance with our classification of direct and indirect taxes in the over-all tax system, direct taxes accounted for 58.3 per cent of all federal, provincial and municipal taxes collected in 1961".

Then you refer to Appendix IV. I think that the most startling aspect of your Table perhaps in relation to the orthodox or the usual method of showing this division is the inclusion of the provincial sales tax as a direct tax. The only indirect taxes which you show in Appendix IV are the sales tax, the excise tax, et cetera, and customs duties collected by the federal government.

DR. PETRIE: Right.

MR. COYNE: Then you say on page 28, about one-third the way down the page:

> "The heavy emphasis of direct taxation in the over-all tax structure, at high levels, appears to be one cause of the decline in personal savings and business capital formation."

I am just wondering whether you are using the term "direct taxation" on page 28 in the same sense as on page 15. Because, for example, if the federal government switched over in the sales tax field from the manufacturer's level to the retail level, let us say, which has been suggested by some, that would mean in your terms a very substantial jump in direct taxation. On the other hand, by the same token it would mean quite a marked shift from taxes on income to taxes on consumption, which is something which you advocate.

DR. PETRIE: That is right. To go back to this point, Mr. Coyne, on page 28, and I am talking about direct taxation, what I really mean is the taxation of income and corporate profits.

MR. COYNE: Yes.

DR. PETRIE: This other matter is purely semantic and we do not need to go into section 92 and talk about whether provincial taxes are direct or indirect, because they have to be direct according to the constitution.

MR. COYNE: That is what I thought was the case with regard to page 28, and on page 15 it is merely a matter of choice for statistical purposes?

DR. PETRIE: Yes, which deviates from national accounting, and I thought we had better make that abundantly clear.

MR. COYNE: Mr. Chairman, I was now going to turn to page 22. Perhaps you or some of the other Commissioners have some points that you would wish to take up in the intervening pages.

THE CHAIRMAN: I think we are all clear up to page 22.

MR. COYNE: On page 22, in paragraph 46 you are talking about business gross fixed capital formation as a percentage of national income, and about a third of the way down the page you say:

> "There is an interesting relationship between government expenditure and business fixed capital formation.

> The continuing increase in government expenditures since 1957 has been accompanied by a continuing decrease in business capital formation".

I just ask you what significance you attach to this. It seems to me that it is perfectly clear as a statement of fact that government expenditures have been increasing and business gross fixed capital formation has been decreasing, but perhaps it is not as clear as to any actual relationship between the two.

It might, for example, be suggested, and the statistics themselves are perhaps equally consistent with the suggestion that if it had not been for the continuing increase in government expenditures business gross fixed capital formation would have gone down even more.

Can you perhaps explain in a little more detail the basis upon which you relate these two trends?

DR. PETRIE: I am trying to imply here, through the use of these data, that the government expenditure side has been accentuated in the consumption sector at the expense of the capital formation sector.

In other words, we are siphoning off, in my view -- again, I am not speaking now for the Chamber; I am speaking for myself -- a great part of

the nation and putting it into the expenditures side, on the consumption side. If this had not been so, I think the capital formation of business might have been larger.

MR. COYNE: Thank you very much, I understand the theory, but would you agree that it is a matter of some difficulty to actually trace the causal connection between the one and the other?

DR. PETRIE: I agree. In this problem of the economist versus the accountant, the economist is on Cloud 9 typically, and all he can do is theorize. But it is my conviction, for the record, that if we had not concentrated so much of the expenditure side on consumption, there would have been more left over for the capital formation side. That is all I am trying to point out.

THE CHAIRMAN: The capital formation side of government, or the private sector?

DR. PETRIE: Both; but principally private.

THE CHAIRMAN: It seems to me I heard Walter Heller say not very long ago that for every dollar that went to consumers they spent 92 cents. Therefore, if government pumped into the consumption stream a lot of money, it would obviously increase consumer spending, according to his statement -- 92% of what went in. The other 8% would be saved, I would assume.

That being so, would that not increase the amount of goods very, very substantially, and that

being the case, would that not have paid off, as far as the private sector was concerned, with a greater demand, and a greater demand with the usual results, which would be increased production and increased employment?

DR. PETRIE: To save your time, Mr. Chairman, I will say that I just do not know.

THE CHAIRMAN: I have not any idea. I was looking for your views on that, because I was very much struck by his statement and I was wondering if economics were just that simple.

DR. PETRIE: They are not. They never are.

MR. COYNE: Mr. Chairman, I was now going to turn to page 24. Here, Dr. Petrie, you are speaking of taxable capacity and the relationship of the size and distribution of the national income to taxable capacity.

In paragraph 50 you state:

"The size of national income is not, by itself, a very meaningful measure of taxable capacity, although within limits it can be argued that the larger the per capita income the greater is the taxable capacity. Thus it appears that if taxation amounts to 30% of national income, such a levy on the 1962 per capita income of $1,641 could be better tolerated than it would have been on

D-5

the 1938 level of $359 per capita."

My question is simply this. I realize that this is a general statement, but for figures of this kind to be really meaningful is it not necessary to take into account changes in the value of the currency during the period?

DR. PETRIE: This is right.

MR. COYNE: It may not affect the validity of the general statement, but it would be appropriate?

DR. PETRIE: Yes, it would be appropriate.

MR. COYNE: If one was going into it in detail, it would be appropriate to take into account changes in the value of the currency?

DR. PETRIE: I would agree.

MR. COYNE: I suppose that would also be true as far as the conclusions which you draw on page 25 are concerned? That is, I put it to you that it could happen that the fact that the bulking of income has moved up the scale from the below $2,000 to the $4,000 to $6,000 level in 25 years could be accounted for in part by simply changes in the value of the dollar?

DR. PETRIE: For the record, I did play around, when I was using these figures, with the deflated, and it is so tricky that I decided not to use the figures but to use current figures.

COMMISSIONER WALLS: Was there any particular reason why you picked out these two

particular years 1938 and 1962?

Would the intervening years have shown any variance in that picture? It seems that those are odd years to use for comparison.

DR. PETRIE: What I did was take a fully pre-war year.

COMMISSIONER WALLS: The last depression year?

DR. PETRIE: Well, 1938 wasn't too bad compared with the standards of the 1930's. But when you take 1939 you are --

COMMISSIONER PERRY: There were still 1,000,000 people on relief in 1938.

DR. PETRIE: But when you take 1939 you are getting to the war, which started later that year, so I took 1938 as a pre-war year. I did the series completely throughout, and to save time and space I just took these two periods.

COMMISSIONER WALLS: Thank you.

MR. COYNE: Turning to page 26, I did have a part marked at the bottom of the page and over on to page 27. I think we may really have disposed of this already. You say:

> "Earlier yardsticks have had to be abandoned in the light of the rate of economic expansion under conditions of very heavy taxation. Yet somewhere there is obviously an economic upper limit to taxable

> capacity, and it is suggested that serious economic distortions occur well before that upper limit is reached".

I think that is the point you were discussing with the Chairman a few moments ago.

DR. PETRIE: Yes.

COMMISSIONER PERRY: There is just one minor point I would like to make. In paragraph 52 you say that taxation is now at an all-time high. I suppose what you really mean there is an all-time peacetime high?

DR. PETRIE: Peacetime high, yes.

COMMISSIONER PERRY: It was certainly higher during the war.

DR. PETRIE: Yes. I mean peacetime.

THE CHAIRMAN: Is that the place where you say that it should not go any higher? No, that is later on, is it not?

DR. PETRIE: On page 27 at the top of the page I say "somewhere there is obviously an economic upper limit", and as I told you, Mr. Chairman, I do not know where the upper limit is. Before you reach that economic limit you will have very serious distortions which probably will not be measured until three or four years after the fact.

In otherwords, you can be digging yourself a grave long before you are dead, and after the grave is dug and you fall into it, then of course

D-8

history will record the sequence of events that put you into the grave.

THE CHAIRMAN: You talk about deficits and say that indicates that we are either unable or unwilling to pay enough taxes to meet our expenses. As to being unable, it seems to me that the net disposable income after taxes keeps going up and we could be taxed sufficiently to pay the deficit.

DR. PETRIE: Here again, Mr. Chairman, I am talking about basically a political philosophy. It seems obvious to this one lone observer that we have had deficits because no government in Canada has been prepared to tax the people sufficiently to meet the costs of government. So we have had very substantial deficits in eight out of the nine past fiscal years.

We are either unable or unwilling, and who is to tell whether we are willing or not, except the people who are elected to run the country.

THE CHAIRMAN: Heaven forbid that we should have higher taxes, but for the life of me I cannot see, on the figures you have given, why, if net disposable income is going up all the time, we cannot have higher taxes and clear the debts.

DR. PETRIE: Supposing we were to meet the deficit of $700 million through increased taxes, the economic distortions would be so great that we would curb our rate of expansion. We might slow it down and get greater unemployment, and I think

D-9

probably this is what political leaders are thinking of all the time.

THE CHAIRMAN: It depends where the money goes, does it not? If money is going to be pumped into the stream somewhere, it would replace, if it was taken in taxes, what would be taken away in loans, I suppose, by people who had put their money into government bonds, but whether that money would be more useful as against the loan money, I do not know. I suppose that is the issue.

DR. PETRIE: That is it. Suppose you add ten points to the corporation tax in order to pay our way. This would slow down the rate of corporate expansion and we would have more unemployment.

THE CHAIRMAN: I think I begin to understand your point.

COMMISSIONER PERRY: This is a point where it is interesting to look at the whole system of government finance. The increase in debt and federal deficits in the last few years is almost exactly measured by the increase in the payments to the provinces.

One could say that in effect the federal government has been taxing for the other two levels of government, or borrowing, rather, for the other two levels of government, and had it not done this the problem would have been left primarily with the provinces as to whether to increase their taxes or increase their borrowing. So perhaps, in

that sense, the federal government is better justified in doing this than to have the provincial governments increase their borrowing. By the same token you might almost say that it is the provincial governments which have not been willing to increase their taxes sufficiently.

THE CHAIRMAN: Yes, Mr. Coyne.

MR. COYNE: Then, Mr. Chairman, I was going to move right through. I have finished with part 1, which is the tax structure today and its problems, and part 2 deals with fiscal and monetary policies and the effect of Dominion-Provincial tax agreements.

On page 34 you give a summary and conclusion related, perhaps, to the point that Mr. Perry was speaking to just now. You point out that the opportunity for full use of fiscal policy, particularly tax policy, was greatest when the major tax sources were centralized in the federal government. Then you say that decentralization has weakened the potential of fiscal policy, and you illustrate that.

Then at the top of the page you state:

> "It now appears that a major overhaul of federal-provincial financial relations is indicated. Under present conditions and the strong pressures for even greater sharing of major tax revenues with the provinces, future federal fiscal

> policy is largely dependent upon a resolution of the important fiscal problem of the division of government responsibilities and the means of paying for them."

I infer that the Chamber is not in a position to put forward any specific suggestions as to how these important political problems should be resolved?

MR. LEACH: I think that is correct, Mr. Coyne.

MR. COYNE: You have stated what you envisage to be the problem and that it requires a solution, but that is as far as you are prepared to go.

Then over the page, and still in this same section, on page 35, paragraph 70, you indicate that tax policy should be used to rectify the longer-run structural changes, rather than short-run cyclical changes, and you state that taxation should not be used in an attempt to stabilize the short-run cyclical variations in economic activity.

Then you say:

> "The pursuit of economic stability by means of frequently fluctuating tax rates appears to be an exercise in futility".

My question is this. Would you propose to eliminate tax changes altogether, or is this merely

a note of caution? I wonder if you might be prepared to comment, for example, on the system recently introduced in the United Kingdom, where the government has been given the power, as I understand it, to vary, within limits, the rates of indirect taxation deliberately as a short-run, counter cyclical measure?

DR. PETRIE: I think what we mean here is a note of caution. Basically the Chamber feels that we should have some stability in rates of taxation so that business planning can be done more easily than if you have a jumping up and down of rates across the board in the middle of a fiscal year for a corporation, and so on.

What I personally mean is that I do not think the tail should wag the dog and that we should get the tax structure fluctuating from month to month or from quarter to quarter in accordance with the fluctuation of the business cycle. I think we should have relative tax stability.

MR. COYNE: Would you distinguish between commodity taxes and income taxes in this field? I believe the British system is limited to commodity taxes.

DR. PETRIE: That is right.

MR. COYNE: On the other hand, it was suggested to us not so long ago that the same counter-cyclical purposes could be served by permitting, within limits, variations in the income tax rates.

Would you consider there is a distinction between the two types of taxes in this respect?

DR. PETRIE: I think, speaking personally again, I would distinguish between taxes on income and profits and taxes on commodities. But, again, I just do not like this idea of having a budget speech brought down in March, April, May or June changing as of midnight commodity taxes, because this gives rise to a state of great confusion and all planning is upset. I would rather have the reasonable assurance of reasonable stability of my taxes if I were a business planner than having to be confronted with a change, say on building materials, in the sales tax, which I think we are all familiar with and as happened on June 13 last, and the problems this has caused.

I think that basically, from the Chamber's viewpoint, all we mean here is a note of caution.

THE CHAIRMAN: Mr. Coyne, might I say to Dr. Petrie that of course we are very interested in this because it is a matter of prime importance to us, the extent to which taxation should be used as a stabilizer.

One of the most outstanding demonstrations, I think, of taxation for this purpose is perhaps the Swedish reserves, where the Swedish reserves, as you well know, are built up over a period and then, by government edict they are suddenly released as a counter-cyclical measure.

They tried this in 1958, and not very successfully; but they were, I believe, very successful in 1962 -- early in the year -- or it may have been late 1961, because they did it really in anticipation of the downturn. It required great Government planning to be able to do that, and I felt they were most successful in that.

Now, in England, again, they tried an investment allowance for this purpose, and they found that it is all very well to encourage activities, but they found that they virtually can't decree them. In other words, the manufacturers demanded that they use stabilizing, and I would have thought that there may be a way that these things can be used.

DR. PETRIE: Maybe in my advancing years I am getting to be cynical, but I do not think that any economic planner, whether private or public, knows beforehand what the shape of things to come is going to be, and by the time you get the upturn or the downturn you have gone by it; and by the time you get the indicators which are two or three quarters late from Dominion Bureau of Statistics, in terms of accounting, even if you are on the inside of Government it may be that the high point has gone.

I am not saying that I am objecting to economic planning, but I do say that the timing is very vital and very difficult because you are not on top of it. It is not as though you were running a company. You are running a complexity of factors which are composed of so many variants that if you decide

you want to increase or decrease taxes and you make a study as to whether it is to be an upturn or a downturn, you are too late by the time you discover it. Therefore I say: Let us not have the tail wagging the dog; let us have some other means such as monetary policy rather than fiscal policy or tax policy, as an economic controlling instrument. I would downplay the tax factor in economic planning and stress monetary policy, because you can do that overnight.

MR. LITTLE: I would like to supplement what Dr. Petrie has said about your remark about the Swedish reserve system, because this is a little different than using the tax structure for control, as Dr. Petrie uses it, and in the sense in the brief; because under the Swedish system the amounts are not taken away from industry and spent by Government; they are, in effect, reserves; and when those reserves are released it is simply permissive for the private company to spend those reserves on a plant of their own choosing; so that there is a degree of choice, and it is private action which results in the release of those reserves.

This is different from talking about using the tax structure...

THE CHAIRMAN: I don't think so, Mr. Little. There is freedom of choice on what you spend money on. There is freedom to spend it. That is the whole scheme of this thing.

MR. LITTLE: Yes; but who spends it? We are talking about Government spending.

MR. KEEPING: I think this is quite clear to the Commission, but I would like to emphasize that when we make this remark in the brief we have in mind not necessarily specifically the rates of tax; we have more in mind, vis-vis the corporate tax rate, the effecitve rate of tax to a certain company.

In other words, we are thinking of incentive legislation being introduced and withdrawn as well as just changes in the actual statutory rates.

THE CHAIRMAN: We are talking about what -- not growth?

MR. KEEPING: Yes, that is right.

COMMISSIONER PERRY: On this matter of short runs, most of the witnesses before the Banking Commission told them that the lags in monetary policy are so long that there is not much you can do with monetary policy. I am afraid you can build it up that the same thing is true of fiscal policy.

The real problem is that you never know whether the short run is the early stage of the long run and whether, looking back a year later, you feel "My God, why didn't we do something about this? It has become quite serious." I think this is the nub of the problem in using these devices.

I gather what you are saying there -- and I agree fully -- is that it is futile tinkering around with the tax system as though it were something with a lot of dials on it which could be geared to conditions as they arise?

DR. PETRIE: I agree. All I am saying

is that this is not an IBM computor. You don't just puch the buttons and get the answer. We want stability. I am an economist and I am representing business, and I want some assurance of relative stability in taxes.

COMMISSIONER PERRY: This derives from the basis of making a case for a tax system which produces a balance at full employment and which is changed very little from year to year, and the deficits appear automatically and the surpluses appear automatically.

MR. COYNE: Is this a good time to break, Mr. Chairman?

THE CHAIRMAN: Yes, I think it would be. We will stand over for ten minutes.

--- Recess

THE CHAIRMAN: Mr. Coyne, we are at Part 3, page 36.

MR. COYNE: Yes.

Mr. Leach, at the bottom of page 36 -- and we are dealing with the "Objectives of the Tax System" -- you say:

"The encouragement of production and long-term economic growth through (1) the maintenance of a balanced relationship between saving and investment on the one hand, and consumption on the other..."

Then, on page 38 in paragraph 75 you say:

"The maintenance of a balance between saving and investment, and consumption

seems necessary to achievement of a healthy and expaning economy. While it would be difficult, perhaps impossible, to determine with precision the proper balance among these factors in a dynamic and ever-changing economy, it seems obvious that consumption and the production should be maintained in some rough equilibrium..."

I think this is the same general subject we were dealing with earlier this morning, and again am I right in interpreting this as simply a general statement as to the objective which the authors must have in view, but without putting forward specific or detailed ways in which this balance can be achieved?

MR. LEACH: That is perfectly right. It shows the area in which he wants to develop the thing.

DR. PETRIE: All I can say is that it is a very broad statement of principle. I don't think that we are qualified to say to any government how it should be done. All we are saying is that there should be some sort of balance.

THE CHAIRMAN: Before you move on, I have noted this word "encouragement." I must say that it concerns me a little bit because there is a maximum that one can do by way of encouragement under taxation. It seems to me that any tax must be an obstacle of some kind. On the other side of the curtain the expenditures of government may be positive things and may do good in many respects, and do; but

when one takes money away -- really all one can do is to take less money from everybody. Taxation is a means of distributing government taxes throughout the nation; and all we can do with production is to take less money away from production. But can we take less money away from production? We still need money. Doesn't taxation -- it discourages activity. This is in the area of semantics, but I think it is important.

DR. PETRIE: The only way I can answer is to say that, of course, all taxes in essence discourage activity.

All that we are trying to say is that the taxes should be more emphasized on the consumption side rather than on the production side. Now, we must remember that we have a fixed level -- a minimum fixed level -- of government expenditures that have to be financed either by taxation or both by taxation and borrowing, and my own personal view is that it would be sounder in the long term to place less emphasis on taxes on production and more emphasis on taxes on consumption.

THE CHAIRMAN: I get that point all right. I just don't like giving the impression that taxation is a buoyant thing. Taxation is a deterrent.

DR. PETRIE: I agree with you one hundred per cent; every tax is.

THE CHAIRMAN: That is the point I wanted to make here.

MR. COYNE: Well, then, turning to page 41, you make an interesting comment on the possible

relationship between high taxation and emigration. In paragraph 79, two thirds of the way down the page, you say:

"Finally, high taxation may have an effect on emigration..."

and at the bottom of the page:

"...taxes in Canada probably have a bearing on it as well..."

We have heard this before, but we haven't seen anything that could be called specific evidence that there is any actual encouragement to emigration in the Canadian tax structure. Do you have any detailed or specific evidence to put forward on the point?

MR. LEACH: No, we have no evidence on it. I think it has been said or suggested several times. It is a general statement, that taxes may have an effect on it. It is just an idea but we have no specific proof.

MR. COYNE: You don't put it forward as a principle...

MR. LEACH: No.

MR. COYNE: ...because of the emigration of professional people to the United States.

MR. KEEPING: However, I do think, Mr. Chairman, if the rate of taxation in the United States were very materially below the rates in Canada it could well have an effect.

MR. COYNE: You are speaking now hypothetically, Mr. Keeping?

MR. KEEPING: Yes. I have no

evidence to show that it has any effect at the present time -- any material effect

MR. COYNE: But you were suggesting that if there were a more substantial difference between the two tax structures then this might have some effect?

MR. KEEPING: Yes.

THE CHAIRMAN: Salaries being 40% less in Canada than in the United States? I think you say that here.

MR. BROWN: That would depend on the point at which you are making the comparison.

THE CHAIRMAN: Salaries are usually 70% in Canada of what they are in the States; but when one gets down to computing the personal income by taking the total income divided by the number of people I think you will find that it is about 30% less in Canada, or about 40% more in the States. You are not proposing that that difference be made up by taxation being less in Canada than it is in the States, because as far as finance goes that would mean more people leaving Canada than anywhere else.

DR. PETRIE: I would think the basic incentive for people moving south of the border has nothing directly to do with taxation; it is more directly due to the higher take home pay that they get in the States.

This is my personal view.

MR. KENT: I think, Mr. Chairman, we feel that we should take extreme care that this gap is not so widened by the impact of personal taxation.

MR. COYNE: Then, may I turn to page 46 -- still on the same Part -- where you are discussing tax neutrality versus discrimination? At the end of paragraph 87 you state:

"While we recognize the impracticability of complete tax neutrality, we submit that deliberate tax discrimination should be avoided in formulating tax policy..."

and you comment on the same subject at page 48 where, towards the top of the page, you submit "...that direct subsidies are preferable to tax concessions and incentive..."

Your statement that deliberate tax discrimination should be avoided in formulating tax policy is somewhat more categorical than similar statements which have been made by others, and taken literally I put it to you that it suggests that all tax incentives should be totally avoided?

I do not think you really go quite that far in the balance of your brief, but I wonder whether you might expand that.

DR. PETRIE: That is right, Mr. Coyne. We have a principle of tax neutrality and we have tried to argue our case. There are perhaps occasions when you can have unneutrality. There may be cases in terms of the national welfare when you do provide certain incentives. But as a basic principle we are saying that we would try to get to neutrality.

This is my own personal view, Mr. Chairman, that if we have to subsidize industry, I would subsidize industry personally directly rather than indirectly, through tax concessions. Because if you subsidize directly, this comes up for scrutiny every time that the budget comes down and people know what it is costing. But you do not know what it is costing when you allow all these gimmicks such as a special capital write-off, and so on. You do not know what it is costing the revenue.

THE CHAIRMAN: I thought that this was in your submission. If so, it is the view of your delegation, is it?

DR. PETRIE: The Chamber concurs in the basic principle that we prefer tax neutrality.

MR. COYNE: I suppose it would also have the advantage of assisting the search for clarity and simplicity, which is another one of the tax principles which you advocate?

DR. PETRIE: Yes.

COMMISSIONER WALLS: Mr. Coyne, could I put a question which is back on page 44, before we proceed further.

THE CHAIRMAN: I have one on page 42. Mr. Coyne was dealing with the whole section. Are you coming back to let us get at the section, Mr. Coyne?

MR. COYNE: Yes, I can do that.

THE CHAIRMAN: I thought that was the plan.

MR. COYNE: Very well, I will go on to the end of this part and then you can ask your questions on the various parts. I see that I have no other question on this part, so perhaps you would like to proceed, Mr. Chairman.

THE CHAIRMAN: Mr. Walls?

COMMISSIONER WALLS: The top sentence on page 44 indicates that the welfare program has exceeded either our ability or our willingness to pay for it. You say that it is your contention that the welfare program has gone too far. That is a widely expressed opinion, of course, but I should like to see if we are thinking along the same lines.

I doubt that any of us feel that it has gone too far as long as there are specific needs which still have to be fulfilled in that way. Is it not that we feel that it is not sufficiently selective today in that family allowances, old age pensions, etc., are paid to people who need neither of them. In fact, that might also apply to unemployment insurance in such cases. It is not that there

is not the need for a welfare program, but it may be that they are not selective enough.

DR. PETRIE: I think Mr. Brown is better equipped than I to answer that.

MR. BROWN: Our attitude on the part of the Chamber has been that we want to see that no Canadian suffers because of the lack of means to take care of his needs or his health and welfare. But we do believe that our desire to be away from perhaps a means tested basis has resulted in the fact that we have carried our programs too far in relation to our current income. This is the problem, as we see it, and this is the problem as we discussed it with Cabinet.

COMMISSIONER WALLS: Thank you.

THE CHAIRMAN: On page 42, at the top of the page you say:

> "Such U.S. tax devices as splitting of income between husband and wife offer upper bracket taxpayers an advantage",

and so on. I notice that you believe that upper bracket taxpayers are too heavily taxed, but I do not believe you make a recommendation as to income splitting. I think the only reference to that is on page 42.

DR. PETRIE: That is right.

THE CHAIRMAN: Have you got any recommendation there?

MR. LEACH: Not on that subject, no.

THE CHAIRMAN: Thank you. I think I will stop there. When I say a recommendation, I mean either negative or positive.

DR. PETRIE: No.

THE CHAIRMAN: Do you support the status quo?

DR. PETRIE: I think we do.

THE CHAIRMAN: Or do you recommend a change, or have you nothing to say?

MR. LEACH: To the best of my knowledge, in our discussions we have supported the status quo. Perhaps we could get into this further when you get to the personal tax section.

THE CHAIRMAN: Very well. I only found it here and that is why I raised it here, but I will make a note of it when we get to the personal tax section and then come back to it, if I may.

MR. COYNE: Then we come to Part Four, which commences on page 52, which deals with the impact of taxation on the economy. The first section deals with corporation taxes. I should like to turn over to page 55, where you are dealing with certain specific impacts of the corporation tax, specifically the creation of new enterprise. You say in paragraph 100:

> "It has been said that taxation considerations 'seldom dominate decisions to organize small independent enterprises'.... In the promotional stages of a new enterprise it is particularly difficult to attract outside capital".

I should like to ask you whether this difficulty of attracting outside capital is, in your view, affected by the tax structure, really by the corporation income tax which we are discussing at the moment, and in what way.

DR. PETRIE: Mr. Coyne, I do not think that the level of corporation tax has a very serious implication here. This creation of new enterprise involves risk capital, and if the corporation tax were 15 per cent or 52 per cent I do not think it would be very important. We merely mention this in passing because it has been discussed by a number of learned writers, and I wanted to give that quotation. You also see the footnote referring to Butters and Lintner and his work.

MR. COYNE: Yes.

DR. PETRIE: I do not think this is a very important point.

MR. COYNE: Would you think that the absence of a capital gains tax in Canada would be a counter factor in the sense that it would have any encouraging effect in this field as against the situation where there was a capital gains tax?

DR. PETRIE: Again speaking personally, we have a capital gains tax in the United States which does not seem to have had any serious impact on the creation of new enterprise. Again, I am not concerned about this.

MR. COYNE: Your principal position is that in your view the tax structure has very little to do with ---

DR. PETRIE: To do with creation.

MR. COYNE: Yes, with creation.

DR. PETRIE: But once you get it going, it has a lot to do with it.

MR. COYNE: I understand that you deal with that again in the succeeding pages.

DR. PETRIE: That is right.

MR. COYNE: In fact, the following section commencing on page 57 deals with the effect of corporation income tax on the expansion of small companies. Then over on page 58, paragraph 108, where you are referring to the two-stage rate of corporation income tax, you say:

> "This procedure seems to be predicated upon the assumption that the corporation, like the individual, has tax paying ability per se".

I wonder whether you would expand on what your meaning is there in view of the fact that certainly when the low rate was first introduced, and possibly in succeeding years, the Ministers of Finance have justified or put it forward simply as a device to help small business.

DR. PETRIE: This was apparently the reason why the graduated rate was introduced. I still say that corporate income is not personal income, because after all a corporation is a legal

fiction, is it not?

MR. COYNE: I would have to agree with you although I am not bound to answer any questions.

DR. PETRIE: I apologize for asking the question.

THE CHAIRMAN: Your answer does not mean that it is not a perfectly good tax by itself though, even though it is fiction for a person.

DR. PETRIE: But the point of difference is that, after all, a corporation is owned by the shareholders. They are the people who ultimately pay the tax.

THE CHAIRMAN: I have a question which I like posing to people, and I think I will pose it to you. If the corporation is owned by non-taxable beings, whether they are a lot of people whose income is not taxed, or a charitable organization, or some other body which does not pay taxes, or even a non-resident if you like, and the corporation in question is fairly prosperous, should it not pay tax?

DR. PETRIE: First of all let me point this out, Mr. Chairman. I am not arguing against the corporation income tax. All I am arguing against is the level of the tax. I am not one of those who advocates the abolition of corporate income tax. I believe that every corporate entity, whether it is publicly owned, privately owned, owned by the Crown or owned by anyone, should pay tax.

That is part of my whole thesis and philosophy on tax neutrality. Everyone should pay tax.

THE CHAIRMAN: Thank you.

COMMISSIONER WALLS: Before we go too far, this is not a question but really an inquiry as to whether you have used a correct word. In paragraph 103 on page 56 you refer at the opening of the paragraph to "The main objectives". Do you mean "objections"?

DR. PETRIE: Oh yes.

COMMISSIONER WALLS: Because it gives entirely the opposite meaning.

MR. LITTLE: I have one reason to go back to Mr. Coyne's statement that the low rate was introduced as a relief to small business, and that this was the reason given by successive Ministers of Finance. I think that this may have been in the mind of the Minister when it was first introduced, but my recollection is --- and I think it is correct because we studied this in connection with our own beliefs --- that this was not a reason given at the time. If I recall, it was put forward by the then Minister of Finance as a step toward the elimination of what he referred to as double taxation, presumably on the theory that the individual shareholders were all being taxed at the same level of income. I think there is no doubt that it has been retained as a measure of help to small business, but this was not, to my recollection, why it was introduced.

MR. COYNE: Thank you, Mr. Little. In the view of the Chamber, I am assuming that one of its purposes is to provide tax relief for small business, has it been effective for this purpose? I notice that you are recommending its retention.

DR. PETRIE: That is right.

MR. LEACH: I think that with all its considerable defects it nevertheless has an attraction.

MR. COYNE: For the purpose of providing releif for small businesses?

MR. LEACH: Yes.

DR. PETRIE: In one of his budget speeches two or three years back I think the Minister of Finance of that day referred to how many corporations were paying tax at the reduced rate and there were a very substantial number.

MR. BROWN: The 1962 figures show something like 68,000 out of 72,000 corporations paid tax on $35,000 or less.

DR. PETRIE: I think Mr. Little was right when he referred back to the original motivation of the graduated rate. It was not so much an incentive now as it was to double taxation, but more recently Ministers of Finance have referred to it as an incentive.

MR. COYNE: I suppose that even initially to the extent it eliminated double taxation on modest levels of income from corporations it was a relief to persons at that level.

DR. PETRIE: That is right.

MR. COYNE: Then you go on on the next page or two to suggest really, as I understand it, certain possible alternatives to the flat rate of tax or rather alternatives to the retention of the low rate. The first of them is an option to permit incorporated businesses to elect to be taxed as partnerships or sole proprietorships. The second one is the suggestion that certain tax free reserves might be set up in the first few years of existence. Is this suggestion that the provision of, if you like, discriminatory tax incentives for small businesses in any way inconsistent with your general stand against discriminatory tax measures?

MR. LEACH: I think the reverse. We are trying to bring about a situation where, having eliminated certain discriminations, we avoid causing others. We are trying to bring about a leveling off of the tax burden as it reaches the shareholder, and where a small company might otherwise find itself in a high bracket, we would give them the choice of electing to be taxed as a partnership. In other words, it would tend to keep the impact of taxation uniform for a given level of income. Do I make myself clear?

MR. COYNE: Yes, Mr. Leach, thank you. You are speaking primarily of the first suggestion, for the election to be taxed as a proprietorship at the option of the taxpayer.

Taking the reserve provision in dealing with the main objections which you have to tax holidays for new businesses, page 56, you point out:

> "It discriminates between and among new small companies and existing small companies which, although established, may be marginal and struggling for survival".

Could not the same criticism be made of your reserve suggestion? Perhaps in this sense, that the reserve will only be of value to companies who have some profits out of which you set aside the reserve. What about small companies struggling along and making losses? Would it not be more equitable and neutral to lend this assistance through some form of direct subsidy running through the tax structure, as for example, by the provision of credit facilities, which I think is done in France quite extensively, for example.

MR. LEACH: That may be.

MR. BROWN: I do not think that it was our intention that these are the only two. They were only suggested as some things which might be done. There are others.

MR. COYNE: But in your view these suggestions would not suffer from the disadvantages that you have spoken of in the more general part of your brief, only discrimination and the like.

MR. BROWN: We think that in the

general picture the assistance to new businesses when getting established is in the national interest, and therefore justifies the exception to the general rule.

MR. KEEPING: It is somewhat less discriminatory than the present legislation.

THE CHAIRMAN: I was curious as to why an alternative would not have been to restrict the low rate of tax on those taxpayers who are small businesses. I think you criticise the fact in here that the benefit of that low income tax rate goes to all the companies, big or small.

I would think an easy cure for that is to restrict it to those that are small, is it not?

MR. LEACH: We have considered that, Mr. Chairman, in various ways, but it becomes very difficult to work out a plan and work out a definition of small business.

THE CHAIRMAN: But you have to do that if you are going to give the right to convert to a partnership?

MR. LEACH: That is right; but there might be a simple definition. We certainly think it requires a great deal of thought. You could make it available to a company with up to 10 shareholders and it would not matter how much or how little income they had; they would have the right to be taxed as individuals, which we think is the just position.

THE CHAIRMAN: Would you permit that with a company like the T. Eaton Company, if they had 10 shareholders?

MR. LEACH: If they were foolish enough to distribute the income among 10 people, they would be welcome to do that.

I come back to something Mr. Coyne said. We think that this particular reserve thing is not a dividend or tax holiday; it is not giving something away. It is simply postponing it and giving a small company the chance to use the funds for a period of time, and then to account for them in taxable income.

COMMISSIONER PERRY: Do you limit

this to companies? I see that your wording is "new businesses".

MR. KENT: I think, sir, it is all within the structure of corporate tax.

COMMISSIONER PERRY: You would not extend it to the business that is not in corporate form?

MR. LEACH: It certainly would not apply to this first alternative. That is automatically done.

THE CHAIRMAN: Except that later on you go the other way.

COMMISSIONER PERRY: I am just wondering how much of this you were working out as a two-way street.

MR. HAMILTON: I think it should apply to business per se, to be consistent, sir. I think we should take that stand.

MR. COYNE: You do suggest that the option should work both ways; that is, the unincorporated business should have the option to be treated as a corporation?

MR. KEEPING: That is right. That is on page 59 -- and vice versa.

THE CHAIRMAN: Would you extend that to individuals? I once found that I could save money by incorporating myself. My partners did not like it, so I did not do it. Just how far would one go?

MR. LEACH: This is where you get

into the problems of definition, Mr. Chairman. An individual who is in a small business, if you like, is entitled to this, or he should be. But then you have to establish a certain standard. If it is incorporated, it is certainly that much easier.

THE CHAIRMAN: I am afraid that whatever we do in this area requires pretty tough definitional problems, as we have now. I would not have thought that we might solve them because of the option of going to a partnership. You would not need to restrict that, I suppose, to one business; you could extend that to all. If a man owned 20 businesses, would you let him have a partnership in each one, if they were all small?

MR. LEACH: I think so, Mr. Chairman.

THE CHAIRMAN: I suppose if a chain store company wanted to incorporate all their stores, they could treat them all as a partnership, and you say that would take care of itself because the shareholders would not want to pay tax on the income?

MR. COYNE: Is there any particular problem here arising out of the fact that the election would be the company's, whereas the persons affected are the shareholders and conceivably the election would be to the benefit of some shareholders and would be a severe disadvantage to others?

MR. LEACH: They would certainly, in my view, Mr. Coyne have to participate in that election decision.

MR. COYNE: I take it that the United States must have solved this problem in some way, because they have a system of election of this kind, have they not?

MR. LEACH: I believe so.

MR. COYNE: Perhaps we might turn back for a moment to the beginning of the brief, page 9 of the preface, where you set forth your formal recommendation in this field. You say:

"--unless effective mitigating provisions are enacted"--

Such as the ones we have been discussing:

"--the 21 per cent rate on the first $35,000 of income should remain in force".

Then you say:

"The rates contained in this recommendation are inclusive of Federal and Provincial taxes".

I think that means you are recommending some reduction in the effective rate in most provinces, certainly in Ontario and Quebec.

Does the Chamber take any position as to which of these alternatives is more desirable? In other words, do you think we should retain the 21 per cent rate and discard these options, or do you think it is preferable to discard the 21 per cent rate and adopt mitigating circumstances such as you have proposed?

MR. LEACH: We arrived at this

decision with some difficulty, Mr. Coyne, because it is a theoretical argument on the one side and there are practical considerations on the other. We came to the conclusion that there are so many small businesses in this country and they are so important, everybody says, that for the time being anyway we should retain some help, some assistance. Therefore we are saying, retain the dual rate until some kind of mitigating provisions can be worked out.

MR. COYNE: You have used the word "until", whereas in the brief you use the word "unless". There is a slightly different connotation to it if you say "until", because I think it means you are recommending, or urging, that alternative mitigating provisions be worked out, whereas the word "unless" is a little less directive.

MR. BROWN: I think the word "unless" is the word we would stand by, Mr. Coyne. In the discussion, as Mr. Leach has said, we had a prolonged discussion on this point, and I think the problem we were faced with was that each such small business situation was so different that it was extremely impractical, in the time we had available, to try to determine what was a good, sound basis to come before you with, Mr. Chairman, and recommend. At least we saw the problem. We thought that there might be another solution. But we did not see what mitigating provisions, how many there might be, could be brought in which would prove effective in the variety of circumstances that apply with these

small businesses across the country.

MR. COYNE: Thank you, Mr. Brown. Then could we turn to the next section under the general heading "Corporation Taxes" on page 62?

THE CHAIRMAN: Perhaps I had better see whether anybody here has any questions. No, we have not.

MR. COYNE: Thank you, Mr. Chairman. You are discussing the effect of corporation tax on corporate financing, and first of all the problem of debt versus equity financing. You say, on page 62 in paragraph 116:

> "There has been much discussion as to the real effect of the corporation tax on management's decision to finance by means of equity or by debt.
> American opinion is not unanimous as to a tax-created incentive for debt financing. It is difficult to provide statistical support for the contention that debt financing has been encouraged by the preferential tax treatment of bond interest. In the United States, developments in corporate financing since the end of World War II do not offer convincing evidence with respect to the impact of corporate income taxation on financial policy. Changes in the composition of new corporate funds are poorly correlated with changes in tax rates. But the basic point is that there is no way of

knowing what methods of financing would have been used if there had been no corporate income tax."

Then going down to paragraph 118 at the bottom of that page, you say:

"It has been argued that tax considerations generally are not dominant in determining the form of corporate financing. But common sense points to the conclusion that when the government pays about half the cost of servicing a bond issue there is a strong likelihood that debt financing has in many cases been decided upon primarily because of this situation".

Let me put this proposition to you related to your point on page 63 that there is no way of knowing what methods of financing would have been used if there had been no corporate income tax. I put it to you that there is perhaps one way of guessing, if one turns to the period, as you have done, when there was effectively no corporate income tax.

You refer, on page 65, to the bond financing spree of the 1920's, and certainly I think you would agree that as far as the 1920's are concerned there was no effect in this area of the corporate income tax as it stood at that level; yet the history of the 1920's, I put it to you, shows a

very heavy reliance on bond financing, in the absence of any tax influences at all.

Why, then, should we be ready to believe that 30 years later, when we have heavy corporate income taxes, a recurrence of the same situation is caused by income taxes?

DR. PETRIE: I do not think we have said that the tax structure has definitely influenced the pattern of corporate financing.

MR. COYNE: I do not think you have, Dr. Petrie; you have been very cautious.

DR. PETRIE: I hedged this very carefully because I just do not know.

COMMISSIONER WALLS: In dealing with this disproportionate amount of debt purchase in the 1920's, was there not an equal equity buying spree in the 1920's? There was, as I remember it.

DR. PETRIE: Not to the same extent as debt financing.

COMMISSIONER WALLS: Maybe I was just hurt by it more.

MR. COYNE: Dr. Petrie, you do take some position on this because you specifically recommend that dividends be deductible for determination of income purposes, in the same way as bond interest. I suppose that would perhaps only be justified, in this area of discussion, if there was a definite effect from the tax treatment upon the method of financing?

DR. PETRIE: I use the words, "common sense points to the conclusion". If I were running a company and I were paying 50 or 52 per cent income tax on my profits, I think I personally would be influenced by the rate of tax in the way I did my financing.

MR. COYNE: If you were running a company and owned some shares in the company, what would concern you would not be the tax effects but the long-term leverage on the stock which you could anticipate as a result of financing your expansion through the bond market rather than by an immediate dilution of your equity interest?

DR. PETRIE: This would be one consideration, yes.

THE CHAIRMAN: Mr. Coyne, I point out that the investment dealers' view of this matter was, I thought, very interesting. They said the same as Dr. Petrie just said, that it is more advantageous to the company to have the opportunity to deduct the interest for securities, and on the other hand the shareholders get a dividend credit. There are two influences working in opposite directions, and really, as far as I could tell, they were reasonably in balance; they did not come down on one side or the other.

But is it not true, when you quote United States statements, one can have regard to the fact that we are more generous in our dividend credits than they are?

DR. PETRIE: That is right.

MR. HAMILTON: Mr. Chairman, we have been talking generally about bond financing versus equity financing, but bond financing is open to a very limited number of companies. A small company might have difficulty in this respect, and a large company might have no further place for bonds in its capital structure and would have to go to preferred or common stock to do its financing. The whole thing has to be looked at in the situation of the company that is affected and I do not think we can accept the fact that any company can be financed by a bond. That is not so, I do not believe.

MR. COYNE: And, of course, these are factors outside the tax structure.

MR. HAMILTON: That is right.

MR. LEACH: The financial markets have an important bearing on this. As Mr. Hamilton has said, there is a point beyond which you cannot borrow.

THE CHAIRMAN: I am very much impressed by the effect of accumulated earnings in this area. As I see it, companies' earnings are something over $1 billion a year. The value of the companies keeps on going up and then they split the stock; and it seems to me that if one accumulates and splits the stock, it is somewhat the same as going out and selling it. It is true that there is a different group of shareholders and they are not subject to the taxes, but as far as getting money into the company, it looks

pretty much the same to me.

COMMISSIONER PERRY: We had quite an interesting discussion on this at one point, and I put the proposition that at the rate that corporations added to investors' equities through accumulation of earnings, if they did not go to the market for bonds fairly frequently the relationship of borrowing and equity capital would very soon get out of kilter.

Then, in fact, there is a pressure on them to borrow.

THE CHAIRMAN: If one adds the $1 billion to the $350 million of equities and contrasts it with the bonds, it seems to me there is a pretty fair proportion of equity money going into companies.

COMMISSIONER PERRY: It is not going through the markets, but it is going into the companies.

COMMISSIONER GRANT: Those who advocate that stocks should be given a better break taxwise in so far as the dividend is concerned -- for instance, that dividends should be deductible as an expense -- might very well be losing sight of the original concept of the corporate structure, in that shares have always been regarded, it would seem to me, as being in the nature of the risk capital; that the person who subscribes to them is taking his chances, with full and complete knowledge in advance that they are subject to being relegated to an inferior position so far as the profits of the company are concerned by

senior debt formations such as bonds, preferred stocks, debentures, bonds in their many ramifications of first mortgage, general mortage, income-bearing bonds and so on.

They know that when they subscribe to the shares in the first instance, but they also know that if the company is successful they may win handsomely. Certainly there are many instances in the corporate life of this country where that very thing has taken place. They have gone in in the first instance at a relatively low price, and they have come out of it at the other end, after a successful corporate existence, with returns which are far in excess of anything they could have made if they had done it with bonds or debentures, where they are told, or assured, that a fair amount of interest will accrue to them in return.

So I think that when we talk about giving the dividend a better tax advantage than it now has, we must not lose sight of the original concept of the corporation.

DR. PETRIE: I would like to point out, sir, that on page 65, in paragraph 120, we are not making a firm recommendation regarding this.

THE CHAIRMAN: I am sorry but what was the paragraph?

DR. PETRIE: Paragraph 120, the last sentence. It reads:

"The elimination of the double taxation of dividends, by allowing a tax deduction for dividends as for interest, would be a

constructive step in promoting more equity financing".

We are not taking a really positive stand there; it is just a suggestion.

THE CHAIRMAN: That is what we are testing. It is certainly what I was directing my remarks to, as to whether this would indicate a constructive step or whether it would not, in fact, push things out of balance.

MR. LITTLE: I think the view of the Committee was that we would not make this recommendation. It may very well be true that the elimination, or the deduction for dividends would be a step in promoting more equity financing, but nevertheless it should not be on the record that the Canadian Chamber of Commerce is recommending to the Commission that dividends be allowed as a deduction.

THE CHAIRMAN: Thank you.

MR. LEACH: I think that is perfectly clear from our opening summary, where we brought forward our recommendations, that much of this is discussion.

THE CHAIRMAN: Yes, I think it is fair that you should remind us that we must not put these things in the form of recommendations, and if we do, please correct us as we go along. I think that this kind of putting a label on it is unfair.

COMMISSIONER GRANT: I have an apology to make. I seem to be giving evidence rather than eliciting it. But I would like to make this observation and get the reaction of the Chamber to it. We have been talking about giving equities a better break, and we have been subjected to a considerable body of opinion that this is necessary because there is a scarcity of equities in Canada today; that the investing public are not being given as wide a choice or as much opportunity as they would like to have to get into the purchase of common stock.

I think that that point was pretty well taken by the Stock Exchange briefs -- both Montreal and Toronto -- in which they felt there was a shortage of equity; and I think within a very short time we had the mutual funds before us, and they came up with a very definite stand that there was no shortage of funds; so that leaves us rather up in the air so far as expert opinion is concerned. Would there be anything you would like to comment on that?

MR. HAMILTON: What I would like to comment is that as trustee of a pension fund, trying to invest money in Canadian stocks and bonds -- and the fund is not very large -- but once you have made your investments and looked down the list of stocks suitable, we very quickly run out of valuable Canadian stocks and I have had to go the the American and United Kingdom market to secure what we are looking for.

This is a limited type of investment for a pension fund, as you will realize, but I do feel that there is a limited range of equity stocks available for that sort of investment in Canada.

COMMISSIONER PERRY: That is what you say in the footnote on page 64.

MR. BROWN: The market supply is limited.

THE CHAIRMAN: When you get down to deal with supply and demand we have had a great deal of discussion on that, but I think it was pointed out to us that on yield stocks our price ratio is not too much out of line with the United States where there is demand and supply, and there isn't a great deal of evidence to

show that the demand overwhelms the supply, or that the supply overwhelms the demand at the present time.

I was rather impressed by the evidence of several people on this.

MR. BROWN: I should also like to underline what Mr. Hamilton said earlier, that the balance between equity and debt financing is important in the structure of our Canadian companies. I suggest that the equity picture can run too far, and we have seen certain companies who have done just that and they have retired them to the point where their earnings were prejudicially affected by it; whereas in others it has been a question as to whether they should be permitted to issue additional equities; but this was necessary in order that they could maintain a proper capital structure.

THE CHAIRMAN: I suspect we all overlook the instances of equity accumulations, and I think if one does this, of course, then the equity creeps up very quickly and the ratio is greatly distorted by it.

COMMISSIONER GRANT: Taking the availability of common stocks, there we are faced, of course, with two things. One is are there enough stocks, or is there enough diversification available through our stock exchanges; and, secondly, are there enough shares of any particular stock, or is there a shortage of shares in some particular stock? The extent that the market -- to use the expression of the brokers -- becomes thin and there are very few

shares one way or the other, will influence prices rather drastically.

MR.HAMILTON: I am not a professional in this field, but I would say that the answer to your question is Yes in both cases. There is not enough diversification and in many cases the number of shares available is so small that one buyer will affect the stocks substantially.

THE CHAIRMAN: But this is not within the general compass of the Canadian Chamber?

MR. HAMILTON: No, I am afraid not.

THE CHAIRMAN: Well, it is interesting, but, nevertheless, we have got an awful lot to do in this brief.

MR. COYNE: I wonder, Mr. Chairman, if we could just look for a moment at the footnote on page 64 -- and this is a small point -- where you state:

"One supporting argument for this view is that a major limitation on equity financing stems from the desire of existing shareholders to avoid dilution of their interest through additional equity issues. We wonder, however, to what extent shareholders of the typical listed company have any choice in the financial policies of their company..."

It seems to me that there may be some confusion here. Clearly the mass of shareholders may have a limited control over the detailed choice as to the method of financing, but would it not be true to say that the

managements who make these decisions are normally shareholders of the companies and therefore have a direct personal interest in adopting policies which will maximise the value of the shares, which is also to the interest of the shareholder?

DR. PETRIE: I think that is right.

MR. HAMILTON: I would agree with that. You are representing the shareholders and you use...

MR. COYNE: And would it not be fair to say that the managements of companies do own shares in the companies in which they have an interest.

MR. HAMILTON: By law they have to have one share...

MR. COYNE: Oh, yes, but...

MR. HAMILTON: ...and they must be concerned on behalf of their shareholders otherwise they are not fulfilling their proper function.

MR. COYNE: Then, Mr. Chairman, I would just like to ask one or two questions briefly on this matter that is referred to at the bottom of paragraph 120. You are not recommending this, but other people have done so. My question would be this: Would it not necessarily follow that if distributed earnings are freed of corporation income tax then the dividend tax credit we know at the moment would obviously have to be eliminated.

MR. LEACH: Oh, yes.

MR. COYNE: Would there also be a problem in relation to the taxation of non-residents. Would it not be necessary, for example, if this sort

of solution were adopted, to increase very substantially the non-residential withholding tax in order to recoup a fair share of the corporate earnings that would be going out to non-residents?

MR. LEACH: That has always been one of the traditional arguments for having taxed corporate incomes.

MR. COYNE: You would agree that there certainly would be substantial loss of revenue if this suggestion were adopted and the withholding tax was left as it is at the moment?

Well, then, in the following section you are referring to the question of retained earnings...

THE CHAIRMAN: Where is this, Mr. Coyne?

MR. COYNE: At the bottom of page 65; and if I might turn to page 67 you say at the top of the page:

> "There is a presumption, nevertheless, that high taxes have in fact discouraged divided pay-outs..."

THE CHAIRMAN: I think that should be "dividend..."

MR. COYNE: Yes; although I suppose it makes little difference --

> "...that high taxes have in fact discouraged dividend pay-outs to individual shareholders in many cases, particularly in the closely-held or family corporations..."

Do you believe that the absence of a capital gains tax

in Canada would also exercise an influence upon the desire of companies to retain earnings in the corporation and thereby build up the ultimate capital value of the shares?

MR. LEACH: This is sometimes claimed. Speaking for myself I am inclined to doubt it. I think it requires...

MR. COYNE: You are speaking here largely, as I understand it, of situations where the shareholders are essentially high-bracket income tax payers and therefore do not wish to receive dividend income on which they pay very high taxes?

MR. LEACH: Yes.

THE CHAIRMAN: If I might interject at this point, I think this indicates that the present tax system is not neutral, and we have heard people saying that they were pressing for neutrality of taxation. If the tax system discourages dividend shareholders -- and you believe it should neither discourage or encourage -- what should be done about it? You haven't made a recommendation?

MR. KENT: The recommendation follows in the section on personal income tax, on the limitations of the graduated rate.

THE CHAIRMAN: Your answer is, then, that it is due to high personal rates and if they were reduced it would probably be a cure?

DR. PETRIE: It is a combination of both.

THE CHAIRMAN: You rest your case

for a cure on reduction of high personal tax rates.

MR. COYNE: Then, on the next page, page 68, you refer to one important factor in this regard as being "...the special depreciation allowances which increased substantially the opportunity of many corporations to retain large amounts of cash, thus reducing dependence on external financing..." I suppose you are referring there to the extent that the capital cost allowances actually exceed what would be claimed under normal accounting practice on the books?

MR. LEACH: I think that is the outstanding example, yes.

I remember querying this very wording at one stage.

MR. COYNE: Then, in the following section, on the effect of efficiency incentives, you state at the outset:

"Furthermore, it is generally believed that a 50% corporate tax rate creates an undesirable psychology about corporate expenses..."

and you develop that in the succeeding page or two, and in paragraph 125 you start with this statement:

"The tax distorts other corporate spending as well..."

Is this sort of thing going to be eliminated if the rate of corporate tax is reduced from 50% to 40%, as you recommend?

DR. PETRIE: I wouldn't like to say that it would be eliminated; it might be mitigated.

COMMISSIONER WALLS: I have one question. This starts off, first of all -- the wording in the middle of the page is "...the psychology of having the government as a 50% partner in the business..." and so on -- and, of course, it really should be "governments." Just before I ask you my question I would like to read a sentence on page 34 where you say:

"There is now the possibility that a general reduction of federal taxes designed to stimulate business expansion could be nullified by a rise in provincial taxes to fill the gap created by federal reductions..." If we are going to talk about federal taxes should we then not only refer to the federal portion in order to talk about the reduction from 50% to the 40%, and take into consideration the 9% abatement that many of the provinces have and the fact that, based on what the provinces are going to ask for in Quebec next month, or in March, it could be a very much larger slice than that; and, therefore, in referring to this as "corporation tax" unless we start considering it in definite amounts as federal revenue you are going to have a tax which will merely be levied for federal revenue. I wonder if we shouldn't stop talking about it in terms of 50% and start talking of what the federal government will get out of this form of taxation.

MR. LEACH: This is one of the key difficulties, with respect, which involves your terms of reference.

It is very difficult to talk about the federal tax only in this sense, that you have to look at the total impact of taxation; and that is the way we have written this text. We feel that maybe it is somebody else's responsibility to define it.

COMMISSIONER WALLS: I realize that. I recognize that the 40% is the maximum that the industry can bear; but is it, then, the effect of your brief that if we are going, as the result of increases negotiated by the provincial government -- this may be a difference in emphasis. You have either got this fixed maximum by the federal government, with negotiations with the provincial governments as to how much they are going to take out and recognize that you have got a fluctuating tax, or you have to look for it to be made up by some other tax rates.

MR. LEACH: I think it is probably inherent in all these figures that there is a 9% or 10% that goes off to the provincial government; and-- members will correct me if I am wrong -- but we might have put this 10 points lower and called it a federal tax.

COMMISSIONER WALLS: Except that one government is now claiming 100% and some of the others are negotiating for something less than that, and one of the problems is that you must then arrive at sufficient revenue, and I don't know if you can arrive at that without having some voice on the amount that the federal government can expect out of this particular tax.

MR. BROWN: If I might say a word here, I think in our approach we have to look at the impact of the total tax structure on the economy of Canada.

It is true that Canada is divided into ten provinces, but as we have said in other circumstances, two of the major problems facing Canada today are the matters of unemployment and the rate of growth, and the way to tackle these questions really is to stimulate industrial growth in our country. Then we have to look at the total picture, and we realize that this creates a problem for you and your colleagues on the Commission who have to look at the matter of taxation in the federal field; but if some action is taken by the federal government which is nullified by one or more of the provinces then it is not going to be long before this action at the provincial level becomes apparent, perhaps, to the industry in the industrial activity and perhaps it will affect the growth, or even the continued employment opportunities, in those provinces if the industry of that province cannot compete in the national picture and, more particularly, in the international picture, because we are a trading nation.

COMMISSIONER WALLS: Would you not achieve this more if you stipulated the percentage of the tax that should go to the federal government rather than the provinces asking for the larger slices; but if it is granted out of the total tax pie then the industries are never going to make any argument.

MR. BROWN: The problem as we see it is the division of responsibility, between the provinces

and the federal government, if the needs of the citizens of the country are under discussion as well as the division of tax revenue; and it is impossible for us to judge where the needs may be divided; and therefore it is impracticable for us to suggest how the tax revenue should be divided.

THE CHAIRMAN: Might I say that the Chamber themselves have quoted exactly the same point as is contained in our terms of reference. We are required to look at all government expenditures.

As Mr. Walls says, we might have seized your point quicker if you had put "50%" and then, in brackets, "40% -- 10% provincial."

It is finally going to be our job to try to produce recommendations to the federal government, which are not completely stupid recommendations in the light of their Dominion-provincial relations, and I don't think we can fairly ask you to help us in this area. We can ask you to help us about the impact of taxation on business, and I think you are fairly trying to do that, it seems to me; but I still see Mr. Walls' point that perhaps it might be better if all the time we kept clear in our minds that this is federal and this is provincial; but we have got ourselves in trouble through having added together our income taxes in one amount.

Perhaps these deficiency agreements that we have had for some years -- there have been a lot of benefits with those agreements, and that is one of the difficulties we have to keep in our minds in the matter of the revenue between the two. But we will make

something out of it.

MR. BROWN: We were reminded by the Prime Minister, when we met with him early last month, that some of the provinces were proposing to take more and more in the health and welfare field. This, as we pointed out earlier this morning, is a very large portion of the increase in government expenditures that have been shown in this field. So that, as we say, it is difficult for us to say just where this is going to show. This is why we thought...

THE CHAIRMAN: I don't think we can ask you to do this.

COMMISSIONER PERRY: And there is a provincial Royal Commission also sitting.

MR. BROWN: Yes.

MR. COYNE: This brings me to the end of the corporation tax section which is at page 70. I don't know whether the Commissioners may want to ask some questions.

THE CHAIRMAN: Yes. I note at the bottom of page 70 you make reference to the administrative difficulty of determining...

MR. COYNE: Excuse me; that is the next section.

THE CHAIRMAN: Is it? What page does the section end at?

MR. COYNE: At the top of that page is the end of the corporation tax section which started at page 52.

Perhaps the commissioners have asked

questions as we have gone along.

THE CHAIRMAN: Perhaps we have.

Well, then, I apologize for the interruption, and please carry on.

MR. COYNE: I just have one or two questions on this section. The first arises out of a statement you make on page 72, where you are expressing your views on the discriminatory withholding tax introduced in the last budget, and you say:

> "Latest official figures indicate that in a 3-months period inflow of U.S. capital has fallen to about $98 million. It had been running earlier to a quarterly rate of $400 million..."

Would it be fair to indicate that not only was there a budget brought down in June, but also that Mr. Kennedy proposed the interest equalization tax in July, and that both of these changes have contributed greatly to this result?

DR. PETRIE: That is right.

MR. COYNE: You are not suggesting this is directly a result of the budget provisions alone?

DR. PETRIE: Not entirely.

MR. COYNE: My other question is simply a general one, the answer to which I think is necessarily inferred, but you criticize the changes which were made in the withholding tax provisions in the 1963 budget. Now I take it that you are recommending that the changes be reversed although nowhere do you in fact say that in specific terms.

DR. PETRIE: I think the implication, even if we did not spell it out, is clear, that we do not like this discrimination which is based upon the degree of ownership of the corporation. I am not certain -- do you know if we have spelled this out, Mr. McNally?

MR. McNALLY: No, I do not think so.

DR. PETRIE: I think the feeling of the Chamber is that we should not have this discrimination.

THE CHAIRMAN: You make a very strong statement in regard to it when you say:

> "In general, it is our view that the use of the income tax as an instrument of economic policy in this fashion is basically wrong."

That is, in the fashion of trying to direct ownership. Well, I suspect -- in fact, you have already said it -- that one of the purposes of the dividend tax credit was to encourage Canadian ownership. That is,a tax to Canadians. Would you not have the same reaction to that?

MR. LITTLE: Mr. Chairman, I think you are quite right in saying that we did not, in our summary of recommendations, take a positive stand on this question, but I think perhaps that that is just an inadvertence; I think, we were in fact taking a position. We did not like the changes in the withholding tax, and our recommendations would be that those should be reversed.

MR. KENT: I might say, Mr. Chairman, that the current policy of the Chamber of Commerce as recommended by its Public Finance and Taxation Committee is unequivocally opposed to any differentiation in the percentage of withholding tax dependent upon any degree of ownership of the corporation as a whole.

THE CHAIRMAN: That is not going anywhere near as far as you go in paragraph 130 where you say:

> " In general, it is our view that the use of the income tax as an instrument of economic policy in this fashion is basically wrong."

I think "in this fashion" means to encourage Canadian ownership as opposed to other ownership is basically wrong.

DR. PETRIE: I think that would be the view of the Chamber.

THE CHAIRMAN: What about the dividend tax credit? When brought in for this purpose, is it wrong?

DR. PETRIE: The dividend tax credit?

COMMISSIONER PERRY: It is being limited to Canadian shareholders.

DR. PETRIE: No, I do not think that is wrong. I think this is a gimmick that was put into the last budget ---

THE CHAIRMAN: I gather you do not like the gimmick. That is clear from what you have said.

MR. KEEPING: Mr. Chairman, is not the basic objective of the dividend tax credit the partial elimination of double taxation?

THE CHAIRMAN: Yes, I recognize that.

MR. BROWN: We have recorded with the government our position with respect to the changes that were made. We recorded them in June, and also before the Senate Committee.

MR. LITTLE: The question of discrimination was raised because it was not available to non-residents, but the non-resident does not have a graduated rate of tax.

THE CHAIRMAN: He is subject to double taxation as, in a sense, the Canadian is. You say that he is charged with the tax on the corporation's income, so he is just as subject to the double taxation as is the Canadian.

MR. KENT: With great deference, Mr. Chairman, that may or may not be so because he may be a non-resident shareholder of a foreign company where his tax is minimal, or even non-existent. In that case his only taxation is the withholding tax. I think it is far more a question of the elimination of the double taxation applicable to Canadians, than any question of impelling Canadian ownership. To that extent, even if it has that effect, then certainly a positive encouragement is far more desirable than a negative one.

THE CHAIRMAN: Thank you.

MR.LEACH: Mr. Chairman, I think we

might just conclude that our failure to arrive at a definite recommendation here is perhaps not a mistake but, rather, an accident in drafting. I think we might apologize for not making our conclusion apparent here.

COMMISSIONER PERRY: The conclusion is that we should revert to the pre-December 1960 position?

MR. LEACH: That is right.

COMMISSIONER GRANT: Before leaving the withholding tax, I wonder if there is any conflict or variance between your position at page 72 where you point out:

> "The balance of payments deficit which has been offset by capital inflows, could have most unfavourable effects on Canada's official holdings of gold and U.S. dollars, and the rate of exchange on Canadian funds."

and your observation at page 23 where at the end of paragraph 48 you say:

> "In the longer term this must be reflected in greater payments of interest and dividends to non-residents, thereby increasing the current account deficit on non-merchandise transactions."?

DR. PETRIE: Would you repeat that question, please? I am afraid I lost you.

COMMISSIONER GRANT: I wonder if there

is a variance in your reasoning, or a conflict in your reasoning, in the statement that appears at page 72. It may be that I have not a sufficient understanding of it. You say in paragraph 129 (3) on page 72 that the balance of payments deficit, which has been offset by capital inflows -- and I take it that the impact of that paragraph is that this capital inflow is a good thing in order to offset the balance of payments deficit -- but then back at page 23 you point out that that balance of payments deficit is exaggerated because of the flow of interest and dividends and payments of the very thing that create the balance of payments deficit in the first place -- that is, a borrowing of money abroad.

DR. PETRIE: I do not think there is a conflict of statement here, sir. We know that the greater our balance abroad the greater will be our interest and dividend payments and, therefore, the greater the impact on our balance of payments position, but I think what we are arguing is that we will have to import, and continue to import, capital at a massive level in order to permit our expansion, and that if we are getting into discriminatory treatment of non-residents' investments in this country, this, in the longer term, will hurt us. In other words, if we argue consistently, then we say that we still want tax equality, and we want to treat everybody alike. My own personal view is that we have to have foreign

capital and, therefore, I argue: "Let us not discriminate against foreign capital", realizing full well that this item of capital inflow has a balancing effect on our balance of payments. It has to balance. I agree with the President of the Royal Bank of Canada when he said: "This is a normal thing for an expanding country like Canada", so I do not think we are inconsistent there.

COMMISSIONER GRANT: I see that you do not rule out either. You say it is something we must have even though it does cost us money.

DR. PETRIE: That is right.

COMMISSIONER GRANT: Because the outflow of our interest and dividends can be offset by other things that that foreign capital generates?

DR. PETRIE: In essence, that is right. What we have to do in the longer term is to export more goods and services in order to pay for our indebtedness abroad. This, I think, is the objective of the government, and of the past governments, and this is a fundamental fact of life. Personally, I am not excited at all about our foreign debits, and I do not think we are inconsistent in these two statements that you call to our attention.

COMMISSIONER GRANT: You do admit that it is a two-way street in this respect, that there are times when the foreign country does not want its money exported. We have had clear evidence of that. We are in a situation today where,

to take the United States and Canada as examples, we do not want their money -- that is, according to government policy -- and they do not want us to have it.

DR. PETRIE: I am not sure that we do not want their money, or that they do not want us to have their money.

COMMISSIONER GRANT: I am talking about the present laws. I am not talking about the attitude of the Canadian Chamber of Commerce. I am talking about the fact that we are endeavouring to keep that money out of Canada.

DR. PETRIE: This is our criticism of the recent budget. We think this is wrong in principle. This is the Chamber's statement.

MR. COYNE: Then, Mr. Chairman, the next section is the one on personal income taxes which commences on page 73. On page 74 in paragraph 134 you make the point that the high upper bracket rates produce relatively little revenue, and they have undesirable economic consequences. Then, over on the next page, in the middle of paragraph 136 you say:

> "Rate progression has concentrated the great bulk of the income tax burden on taxpayers in the upper income brackets."

Now, there is an apparent inconsistency here which, perhaps, merits a comment or an explanation.

MR. KEEPING: I think it hinges on the

word -- at page 74 we say "the higher upper bracket rates", and at page 75 we refer to just "the upper income brackets", and I think that is the fine distinction.

MR. COYNE: Thank you, Mr. Keeping, and this, perhaps, could be related to your recommendation for a cut-off of the ---

MR. KEEPING: Yes. For instance, I think you would consider incomes in the vicinity of $25,000 and $30,000 as upper income brackets, whereas in our recommendation we recommend a tax not in excess of 60 per cent, and that falls somewhere around the $90,000 a year income. I think you have to use that figure when you are talking about high upper braćket rates.

MR. COYNE: Thank you.

COMMISSIONER PERRY: I am going to try out the approach we have had taken by some people before us, and that is that the area in which the rates are most progressive is that of the lower limits of the rate. The Canadian Congress of Labour, for example, pointed out that the progression in the first $5,000 or $6,000 is the same as it is on the last $300,000. If you are trying to reduce the sharpness of progression you should start at the bottom and not at the top. What really bothers me is the importance that people attach to the 80 per cent rate which must be paid only by one or two people in this country, if even that. Do you have any views as to what the rate should be for what Mr. Keeping has just referred to

as not the high income group but the upper income groups -- those earning, say, $20,000 to $40,000? What should the rate structure be in that area? It is about half now. This is a pretty strategic section of the business community.

MR. KEEPING: We have recommended, as you are aware, an overall 10 per cent reduction across the board. In other words, we recommend scaling each of the brackets down by approximately 10 per cent. I have prepared a rough indication of what we had in mind, just to give you some idea. I do not know whether you would be interested in seeing this.

THE CHAIRMAN: Yes, indeed.

--- (Copies of document distributed.)

MR. COYNE: Mr. Keeping, I note that you refer to the 60 per cent maximum which you recommend as coming into effect at approximately the $90,000 level -- that is, after giving effect to your 10 per cent reduction all along the line.

MR. KEEPING: That is right.

MR. COYNE: Under the present structure you reach 60 per cent marginal rate at $60,000 of taxable income.

MR. KEEPING: Yes, if my arithmetic is correct, that is the intention. I would like to offer this only as a possible illustration of what we had in mind. You will note, Mr. Chairman,

if you look down the marginal rates, that they are reduced by about 10 per cent, and also that the quantum of tax at the top of the bracket which is shown under the headings "Present Structure" and "Revised Structure" represents a decrease in the quantum of tax of approximately 10 per cent. You will note also that we have put alongside that comparison of the present structure with the possible reduced structure the proposed United States tax as proposed for 1965 in the House Ways and Means Committee of the United States Congress. We have also shown that in three categories for the individual, for the joint return, and for the head of the household.

One should, of course, be very careful in trying to make any comparison between the effective income tax in the United States and that of our own case, because as is pointed out in the notes there are many areas of difference in computing the tax. There are differences in determination of taxable income.

Another very important point is that our rates as they are given there include the vast majority of our provincial taxes, whereas the United States rates do not include State taxes. There is also the question of dividend credit which is much larger in this country than it is in the United States.

However, we thought it might be useful as a rough guide to show what we had in mind. We

do feel that although as we said earlier we do not think that present rates of taxation as compared with those in the United States have any really matterial effect upon immigration, this is something that we feel should be watched; that they should not become too far out of line, because they could become a factor. The type of personnel with which we are most concerned are those in the managerial, supervisory and technical fields -- people who probably fall into the $12,000 to $40,000 bracket, or that vicinity.

I think we have had that in mind, and I think this is an area that needs to be watched. You will see that our rates which we suggest parallel perhaps more closely the head of the household rates in the United States than the joint return, which is generally lower. Am I taking up too much of your time, Mr. Chairman?

THE CHAIRMAN: No, not at all.

MR. KEEPING: We also split down into the $2,000 bracket the area between $12,000 and $14,000. I am just handing you up a sheet which will illustrate this.

THE CHAIRMAN: The proposed top U.S. rate is 75 per cent.

MR. KEEPING: I think 70 per cent, speaking from memory. The original Kennedy recommendation was a top rate of 65 per cent in 1965, and I think the House raised it to 70 per cent.

If you would just look at this sheet, I have selected this range because I feel that this is the range where possibly there could be some danger from the effect of tax on emigration. Incidentally, I should make it quite clear that I have only used the proposed U.S. joint return, which is the most favourable one and the one I would say was more generally applicable.

Now, take, for instance, a Canadian with a taxable income of $16,000. He presently pays a tax of $4,520. One can say that that is

perhaps comparable, as I think you mentioned earlier, to a taxable income or a salary range of $20,000 in the United States. You will see that in the United States his tax at $20,000 on the basis of the joint return would be $4,380. In other words, he could move from Canada with a taxable income of $16,000 to the United States with a taxable income of $20,000 and get the whole of that $4,000 free of tax. So we think it is important to ensure that our tax rates do not get too far out of line with the United States.

THE CHAIRMAN: That is a good point, but as far as I know Canada is about the only country which does not either aggregate or split. However, you said that we could discuss that later on. Perhaps this would be a good time to break, Mr. Coyne?

MR. COYNE: I think it might be, but I am not sure that this would not be a good time to pick up the point to which you were referring if you want to explore it further, Mr. Chairman.

THE CHAIRMAN: All I wanted was an answer from them whether, first of all, they were against it, or secondly, whether they were for it, or thirdly, whether they were just not recommending it.

MR. KEEPING: We are not recommending it. That is really the position. I do not think we felt that there was sufficient pressure from our membership, or study made of it, to recommend it.

THE CHAIRMAN: Are there any further questions on the tables? If not, I think this would be a very good time to break. We will stand over until 2.15.

--- Luncheon recess.

--- Upon resuming at 2:15 p.m.

THE CHAIRMAN: Proceed, Mr. Coyne.

MR. BROWN: Before we proceed may I offer the sincere regrets of Mr. Little at his having to return to Toronto. The communications system was such that he found he could not delay his departure. He has another engagement in Toronto.

THE CHAIRMAN: We regret it very much, but we understand.

MR. COYNE: I think we have reached page 76. We were discussing personal income taxes. We have dealt with the sections commenting on the economic effects of the tax, and the tax in relation to distribution of the income, and the next section deals with the effect of the personal income tax upon capital accumulation and investment. In paragraph 139 you say:

> "The impact of the tax on the amount of personal saving is clear enough."

And you append in a footnote a summary of Appendix XI, aggregating the figures for two different periods of years. But, if I turn to Appendix XI I find some difficulty in equating the statistics in it with your statement that the impact of the tax and the amount of personal saving is clear enough. In fact I put it to you that some persons might look at Appendix XI and think that the impact was singularly unclear.

For example, if one looks at the trends

in the percentage of personal gross income saved the most remarkable change seems to have occurred between the years 1926 and 1930 when this percentage rapidly declined from 27.9 per cent of disposable personal income to 14.8 per cent. I think it would be agreed that that was a period during which personal income taxes were relatively not a factor. Could you perhaps comment a little further on the conclusions which you seem to draw from the figures given in Appendix XI?

DR. PETRIE: If you take the period from 1926 to 1930, Mr. Coyne, you will note that the percentage of gross personal income saved was 22.7.

MR. COYNE: That is, for the period as a whole?

DR. PETRIE: Yes, for that period. Then, you come down to the period from 1946 to 1951, and that figure goes down to 7.2 per cent of gross personal income saved. Then take the period of from 1952 to 1962 and you see that 5.9 per cent of gross national income was saved. In other words, all I was trying to point out there is that there is a diminishing part of the gross personal income that is being saved.

MR. COYNE: On the other hand, I suppose if one chose some different years one might come to a somewhat modified conclusion. For example, if you take the percentage of gross personal income saved in each year from 1952 to 1962, although the over-all trend is upward it did decline in one year, then went

up, and then declined again, and then rose to a new peak.

DR. PETRIE: Yes, but nevertheless the over-all trend is down, and that is why I spelled out each year. In those earlier years when income tax was not a factor -- that is, from 1926 to 1930 -- it never went below 14.8. Then, from 1946 to 1951, it never recovered, and in the period from 1952 to 1962 it never got as high as it was in 1951.

Now, 1950 was an extraordinary year because of the Korean war. If you eliminate 1950 from that series 1951 to 1961 your average would be much higher than 7.2. Now, it has swung back upwards a little bit, but even so in 1962 when personal saving was at its all-time high related to gross personal income, it is still much smaller percentage-wise than it was before, except for these extraordinary years.

THE CHAIRMAN: Mr. Coyne, might I interject a question at this point?

MR. COYNE: Yes.

THE CHAIRMAN: It would seem to me to be very easy to understand the impact of income tax on net disposable personal income. It has got a very clear effect on that. But, as to savings it seems to me that that is entirely different. Savings represent choices made by people and by business as to whether they spend money or put it aside. So, I would have thought that fluctuations in net disposable personal income caused by taxation could not be said to find their way all into savings. Maybe the choices are

distributed as between spending and saving, but I would not have thought it fair to say that it all was reflected in savings.

DR. PETRIE: I would not like to be on record as saying that you can draw definitive conclusions from this series, but I do think that the trend is pertinent to our argument that income tax had an impact on savings. Whether or not people have decided to spend more or save more is not quite the point. The point is that they have relatively less to save or to spend than they had before.

THE CHAIRMAN: I see that net disposable personal income is directly affected by it.

DR. PETRIE: Yes, that is right.

THE CHAIRMAN: And after that the choice is the individual's.

DR. PETRIE: That is right.

MR. COYNE: Then turning over one or two pages, and still in this same section, you comment on the scarcity of equity capital in Canada. This is something that was touched on this morning, and it has been discussed, of course, by many others. In the middle of paragraph 142 you say:

> "In other words, the corporation tax structure has caused a shortage in the supply of equities and has created a trend for other types of investment such as bonds, mortgages and real estate. Under the circumstances, it was almost inevitable that such a large

> part ... of Canadian enterprise should be foreign-owned or controlled. Canadian taxation has encouraged foreign ownership ..."

Just testing this for a moment, I put it to you that there may be an inconsistency here. I would have thought that it would be in circumstances where there was an overabundance of equities beyond the capacity or the willingness of Canadians to purchase that you would have a tendency towards foreign ownership. If there is a shortage of equities surely it means there are not enough to go around for those Canadians who want to buy them. I think this is the point that Mr. Hamilton touched on this morning with respect to the problems that pension and trust funds find in this field. Would you comment on that?

DR. PETRIE: I think there is no doubt that there is a shortage in terms of the demand for pension funds and other investment groups -- there is a shortage of equities.

MR. COYNE: But does that shortage have any effect upon foreign ownership of Canadian stocks?

MR. KEEPING: May I interject? I think possibly, Mr. Coyne, if you look at page 114, where we summarize the conclusions on personal income tax -- I think perhaps we are getting a little involved in available supply. I think there we say the resulting reduction in available investment funds from private sources for equity securities has been a factor in the large degree of foreign ownership of

Canadian enterprise. I think that expresses better what we are trying to say. It is at about the middle of page 114 under the heading "C. Personal Income Taxes", and it is the third sentence starting with the words "The resulting reduction in available investment funds..."

MR. COYNE: Thank you Mr. Keeping, but it seems to me that you are dealing there with a shortage of investment funds in Canada, and at page 79 -- perhaps I misread it -- you seem to be dealing with a shortage of equity securities.

MR. KEEPING: That is right. I think this is really a summary -- what you are looking at at page 114 and the foregoing pages expresses better, I think, what we really want to say.

COMMISSIONER GRANT: Would it be a correct statement of your submission to say that if we had a more favourable tax climate in Canada for common stocks that more companies would be launched in Canada buy Canadian capital and that therefore United States subsidiaries would not get the foothold which they have at the present time? Is that the conclusion to be drawn?

MR. KEEPING: I do not think so.

DR. PETRIE: No, I do not think this is really the conclusion that you reach. There are two factors, the first of which is that we just have not been able to accumulate the reserves for investing in Canadian enterprise that we might have had because of taxes; the second is that there is a predisposition,

I am afraid, of Canadians to favour the more "secure" securities. The Americans are more ready apparently to put risk capital into a Canadian enterprise. This is why so much of our resource development has been American sponsored.

THE CHAIRMAN: Dr. Petrie, have you any idea of the distribution of equities in Canada as between the various kinds of holdings? It seems to me that there is something between 20 billion and 30 billion of listed securities of the Canadian exchanges.

DR. PETRIE: That is right.

THE CHAIRMAN: I think as far as I can recollect that a pretty small proportion of that is held by institutions. That has been tabulated before us, and that figure is relatively small.

DR. PETRIE: That is right.

THE CHAIRMAN: And a good deal of that is held outside the country, but I think we are left with a very large proportion of it being held by Canadian individuals. Am I not quite right?

DR. PETRIE: Yes, I would think that the whole effect of this ---

THE CHAIRMAN: Have you a tabulation?

DR. PETRIE: No. I think we have made a comment that there is no reliable estimate of the distribution of equities, but holdings by Canadian individuals must be relatively small.

COMMISSIONER PERRY: Dr. Petrie, I was apprised of this about a week ago, but during the

last week I read an article in the December, 1963 issue of the Journal of Finance written by a couple of Canadian professors in which a very simple mathematical calculation was made. They capitalized the amount of dividends recorded for Canadian income tax purposes by individuals, which is something of the order of $300 million plus. The factor that they used was the average of Canadian yields determined by authoritative sources, which was about 3.7 per cent. They arrived at what to me was a rather startling conclusion, namely, that Canadian individual taxpayers held 8.3 billions of equity stock. This is far more than all of the total of equities held by institutions. It is considerably more than the equities held by institutions ---

MR. KEEPING: Of course, this would include private companies as well as those listed ---

COMMISSIONER PERRY: It would include all companies, including foreign companies. The thing that is very indicative to me -- this, at least to my thinking, indicates a greater willingness on the part of Canadians to hold equities than as of a week ago I would not have thought possible.

DR. PETRIE: I have not seen the article, but what you say surprises me.

COMMISSIONER PERRY: The arithmetic is simple. In other words, you multiply $300 million of dividends by 25 or 26 and you get the 8 billions. You would take no account of equities on which no dividends had been paid, or equities with respect to

which taxpayers were not properly reporting their dividends. I admit quite frankly that this came as quite a revelation to me. I think I would subscribe to your statement, but I must say I have changed my views somewhat as a result of this figure. There is not much argument about the arithmetic. If anything it probably indicates a conservative figure.

DR. PETRIE: Well, I agree with you. You state that a week ago you would not have quarrelled with my statement, and up until now I would not have quarrelled with it either.

COMMISSIONER PERRY: I think we have missed some device for making some sort of an estimate of Canadian holdings.

DR. PETRIE: Of course, this ignores direct United States investment, does it not, Commissioner Perry?

COMMISSIONER PERRY: These would be bits of paper held by Canadian individuals -- that is true -- but it still means that Canadian individual taxpayers must be holding something of the order of eight billions of equities on which they are receiving dividends. I do not know that this changes anything in your argument at all. I am bringing it forward mainly as an interesting exhibit for economists.

DR. PETRIE: I am glad that you have this information because, as I say, I have not seen the article.

COMMISSIONER PERRY: The mathematics involved are so simple that it is rather astonishing

-10 that it has taken so long to work them out.

THE CHAIRMAN: It shows that Canadians as opposed to institutions are holding a quite a lot of equities.

MR. COYNE: The figure, Mr. Chairman, is exactly equal to the total of all personal savings deposits in the chartered banks, taking this figure given at the top of page 79.

MR. BROWN: May I ask Commissioner Perry whether those are figures for Canadian dividends, or are they from some other source?

COMMISSIONER PERRY: No, they would be dividends from all sources.

MR. BROWN: It could still mean that there is a paucity of equity capital for investment in Canada.

COMMISSIONER PERRY: I do not think it affects that argument, but it bears on the other side of the argument as to willingness of Canadians to invest in equities.

MR. BROWN: Yes.

THE CHAIRMAN: I think it makes the point that there is a lot of personal investment in equities whereas I think we have been inclined to think it was all institutional investment. It is very far from that.

COMMISSIONER GRANT: The crux of this, Mr. Coyne, would seem to me to be in the statement that under the circumstances it was almost inevitable that such a large part of the Canadian enterprise

should be foreign-owned or foreign-controlled. Now, I have satisfied myself of one or two things here. One is that this is not aimed at starting industries. The lack of response to Canadian equities is not in getting industries started; it is after industries have been well launched. I think we have clarified that, have we not, Dr. Petrie?

DR. PETRIE: That is right.

COMMISSIONER GRANT: Secondly, I think you have said that you would not personally point that dividends should be accorded the same tax treatment in so far as expenses concerned as is accorded to bonds.

DR. PETRIE: That is right.

COMMISSIONER GRANT: Therefore, I am wondering where that leads us. If it is a serious problem which has to be met, how are we to meet it?

DR. PETRIE: My point, Mr. Chairman, is simply stated as follows, that if it were not for the very high rates of personal income tax there would then be more savings available for investment in Canada.

THE CHAIRMAN: Yes. I do not think that there is much the matter with that statement. It has been repeated many, many times to us.

COMMISSIONER PERRY: There would be more money for savings and for investment. There is no *a priori* reason why people would save it rather than spend it.

DR. PETRIE: That is right. They still

have the choice of either spending it or saving it, but if we have a lower rate of personal income tax we would have a choice whereas now we have very little choice.

COMMISSIONER PERRY: I think this is obvious. I do not know why we are arguing about it.

THE CHAIRMAN: I agree.

MR. COYNE: Mr. Chairman, I have nothing further on the personal income tax section, which closes at page 80.

THE CHAIRMAN: Well, I have, and I guess we all have. Certainly when it comes to incentives I am not always impressed by the idea that if you impose taxes people will work less. I have the idea that if you put taxes up people will work harder to maintain their living standard. I think there is as much to that argument as there is to the diminishing returns argument that we hear so much about. When I started these hearings I thought, as you did, that initiative is diminished, but I have an idea that they are ingrained living habits that necessitate our working two hours to get what we need if we find that we cannot get it with an hour's work. Is there not as good a case to be made for that side as for the other side?

DR. PETRIE: Your colleague, Commissioner Perry, and I used to argue about this in the old days.

THE CHAIRMAN: This is not an original thought of mine.

DR. PETRIE: All I can say is that there is a good argument for both sides, but I think when I last appeared before you I said something to this effect, that for me personally when I figure that I work on Saturdays and Sundays the government will get 55 or 60 per cent of what I make then I will not work on Saturdays and Sundays.

THE CHAIRMAN: But if you had to get along without something that you could not get without working on Saturdays and Sundays it would be a different matter.

COMMISSIONER WALLS: I would like to deal with something of a different matter which is on page 80. You say:

> "... for some there is a preference for leisure or tax-free work at home rather than to more 'on-the-job' work at a higher marginal rate of taxation. The economic importance of the disincentive to produce one's full potential output may not be great. But every man-hour lost because of taxation is lost to the national product for all the time."

Surely this is not so if it results in reducing unemployment? In other words, if these people do not expend the time that is necessary for jobs then it is naturally going to increase employment, is it not? Is that not one of the things we are striving for at the present time?

DR. PETRIE: It does not necessarily

follow, Mr. Walls.

COMMISSIONER WALLS: Nothing necessarily follows, but is not that as logical a supposition as you have made in this ---

DR. PETRIE: In this whole area, frankly I have my tongue in my cheek, but I do think that a great many people in this country, and not the salaried people, have no choice really. They are going to work regardless of taxes. But, you have an area of people who can choose to work or not to work, such as married women. When the tax bite gets to the point -- I know this from my own experience because I have had Office Overload people working for me -- when it gets to the point of removing the married status exemption then a woman will stop working for the rest of the year. I think this is wrong.

COMMISSIONER WALLS: You said you had Office Overload coming in to work for you. Does not that mean that you have created more employment for somebody else? The fact that they decide not to work as much as they could has created further employment for somebody else.

DR. PETRIE: I do not think it follows.

THE CHAIRMAN: Surely, it is arguable, Mr. Walls, that when a woman carries on work it may be either good or bad. After all, what are we working for? We are working for consumption and leisure. Is not that the result of our efforts -- to achieve leisure at some time, or to obtain a

15 greater consumption? If we can achieve leisure somewhat earlier than so much the better.

DR. PETRIE: Might I make a humble suggestion? Some people work for pleasure.

THE CHAIRMAN: We are in that field of economics.

DR. PETRIE: Pleasure is an economically measurable quantity.

THE CHAIRMAN: I think I call that leisure. I see what you are saying. You are saying that despite getting paid for it you like to work.

DR. PETRIE: That is right. There are certain people who cannot be idle.

THE CHAIRMAN: You are taking me into a philisophical area that is beyond me.

DR. PETRIE: Please forgive me.

THE CHAIRMAN: I think all we can conclude is that the case is not clear one way or the other.

DR. PETRIE: To clarify the record, if I might just for one moment, I say that the disincentives to work resulting from high income taxation are not of primarily importance across the country on the broad front. In certain sectors of the economy they may be. That is all.

THE CHAIRMAN: Is there anything further with respect to this area of income tax? If not we will go on to capital gains which is something we are all anxious to talk about. Mr. Coyne?

MR. COYNE: Thank you, Mr. Chairman. This section commences at the bottom of page 80, and you

16

commence at paragraph 145 with the statement:

> "In principle 'capital gains' are supposedly tax-free in Canada. The problem turns on the determination of what constitutes a capital gain as opposed to taxable income."

Then, several pages further on you discuss what you consider is the uncertainty in the present legislation, and I would like to return to that a little later. But, just dealing with the inference that you make here, which suggests that they are not as tax-free as we think they are, I would like to ask you to expand, perhaps, a little on your meaning of "capital gains" in this context, bearing in mind this proposition that surely all that we are doing in Canada at the moment is taxing speculative gains. In economic and social terms why should such specualitive gains be exempt? I put it to you that the only difference that has developed in recent years is that what has always been the law has been somewhat more vigously enforced. Is it fair to draw a distinction, or would you agree that there is a distinction between a capital gain and a speculative gain?

MR. LEACH: Yes.

THE CHAIRMAN: To spark this I might say that in my recent travels around Europe I found nobody, as well as I can recall, except perhaps in Germany, who said they were taxing capital gains. Virtually all said they were not taxing capital gains, and I am including the United Kingdom in that.

They all said that they were taxing speculations.

MR. LEACH: I do not think we would disagree with that. I think we have said we want to leave capital gains free of tax, but the problem of defining capital gains is one that we must solve. I do not object to taxing specualitive profits. The trouble is that a lot of people feel that a specualitive profit is a capital gain, and you get into this whole area of terrible uncertainty. That is the thing I complain about.

MR. COYNE: You say that that is what you complain about, but I take it, Mr. Leach, that the Chamber is not in that position. Let me put it to you this way; leaving aside the details for the word definition which obviously give rise to difficulties when you are at the borderline between one or the other, is it proper, as we do now, to draw a distinction between capital gains which at the moment are not taxed at all and what are frequently referred to as specualitive gains from trading activity which are taxed as being income under our present law. Is this a sensible division?

MR. LEACH: I do not know if I have got your question correctly. Capital gains are tax-free, and specualitive gains are taxable?

MR. COYNE: Yes.

MR. LEACH: Yes, I think there is that distinction.

THE CHAIRMAN: Does our law make the right distinction?

MR. LEACH: Our law is a little bit vague in terms of understanding by the average person. In fact, the average person does not know it exists. Consequently, they think that any transactions concerning land, or anything else, is automatically a capital gain.

MR. COYNE: Is that an uncertainty that the law has to pay any attention to? It is certainly a matter of misunderstanding or ignorance on the part of the taxpayer. Mr. Chairman, since this topic comes up later may we turn to it now? It is referred to at page 93 and subsequent pages. I put it to you, Mr. Leach, that in the case of at least 99 per cent of gains the law is perfectly clear as to whether a particular gain is of an income or a capital nature. There is a borderline area which is not clear, and which is the cause of all the recent litigations. But, as compared, for example, with the uncertainty -- and you deal with this subject under the title of "Uncertainty" -- of many of the other provisions of the Income Tax Act -- whether or not a benefit is taxable under Section 8, for example, the question of whether a gain is of an income or a capital nature I might also say is crystal clear and the model of simplicity.

MR. LEACH: I would not want to agree with you 99 per cent, really.

MR. COYNE: That is very arbitrary.

MR. LEACH: I think the feeling of the community is that some way or other there ought to be

some clarification, and the only solution we can arrive at is something like the system in the United Kingdom where there is some rule laid down, and where a lot of these cases can be settled on the basis of what the law says.

THE CHAIRMAN: Do you recommend a time test?

MR. LEACH: We have not put this into our brief, but I know that Dr. Petrie has had dealings with this subject, and he has almost persuaded us that some kind of a time rule would be the best solution. Officially, we are against a capital gain tax for the many reasons that are mentioned here, but the great difficulty -- and I come back to this fact -- is to agree on what a capital gain is, so you are led to the position of having to make some definition in terms of time.

THE CHAIRMAN: The only choice that we have that I know of -- and I say this from having listened to what has been said during these hearings -- is to say with what we have, or something close to it. This is a woolly area. Mr. Coyne says it is not a big woolly area, but there is a woolly area there. Or, we can move to a time test, and certainly every country that I know anything about outside of Canada has a time test.

Sweden has a variable time test, and the others have fairly positive time tests. But, they have all got that and they determine this question on that. People who are opposed to that are inclined

to say that that is so arbitrary that you will bring in things that ought not to be there, and you will leave out other things. But, your view is that you would favour a time test as opposed to what we have now?

COMMISSIONER WALLS: I think Mr. Leach said Dr. Petrie said that. I think we should explore ---

THE CHAIRMAN: I would rather explore what the Chamber has first. I want to know if the Chamber has a view. If they have not, then that is fine.

MR. McNALLY: We have no view.

MR. KEEPING: That is, with respect to capital gains tax.

THE CHAIRMAN: That is fair enough. Now, Dr. Petrie, would you like to explain your position?

DR. PETRIE: I think I did this two months or more ago when I did set up a time test of real estate transactions. I think you will recall that.

THE CHAIRMAN: That is right, I do.

DR. PETRIE: The Chamber does not concur in my views, naturally. I still think that a time test is preferable to the situation with which we are now confronted.

THE CHAIRMAN: You have expressed your views. I wonder if anybody else would like to express a personal view, keeping it outside the views of the Chamber, now that you have been good enough to express yours.

MR. LEACH: My personal view has been,

-21

certainly so far, that the present situation is not bad in terms of the law and the jurisprudence, but I find myself continually under attack from people like our friends here who say it is not good enough. I say that if a man is speculating he should be taxed, but this is a darned hard thing to administer.

DR. PETRIE: I think, Mr. Chairman, a good deal of this problem hinges upon the taxpayer's conclusions. I gave my colleagues in the Chamber an example the other day of a farmer who, in his ignorance sold the wood from his woodlot to a lumberman, who moved in a portable mill and cut all the wood off it for "x" thousands of dollars. Through misadventure somebody from National Revenue happened to see the cheque cleared through a bank, and the farmer was assessed. He then came to me in trouble, and I said "If you had been smart or sophisticated you would have sold the land including the wood , and then had a gentleman's agreement to buy the land back for a nominal sum". But, how is a farmer going to know of these intricacies of the Act. Here is an imocent man who acted in good faith assessed an amount which almost ruined him because he had already spent the money that he got from his alleged capital gain, in his outview, on building a barn, so that he did not have any capital left -- any free capital, any working capital, left.

THE CHAIRMAN: The law should be corrected so that he could do that?

DR. PETRIE: Yes, certainly. My basic

complaint is that if you and I as businessmen propose to go to a venture we really do not know whether the profits from this is income or whether it is capital, and we are in the laps of the gods. I do not like this as a taxpayer. I would like, if it is humanly possible, to have more clarification so that I know before I go into an adventure in the nature of trade, as the Act says, whether I am going to be taxed or whether I am not going to be taxed. This is my major complaint.

THE CHAIRMAN: You have almost convinced me, and I wish you had managed to persuade your associates to speak with one voice. Thank you very much.

MR. COYNE: Perhaps I might pick up one point at page 94 where you are dealing with this subject, and where you say in paragraph 166:

> "We have referred already to the unpredictability of tax treatment in many transactions, the increasing possibility of their being treated as taxable income at very high rates, the lack of any allowance for capital losses..."

Is that strictly speaking correct, that one is not entitled to deduct business losses from business income if they happen to arise out of a speculative venture?

DR. PETRIE: Let us take the case of the real estate transaction which is so often now being

brought into taxable income. If you buy a piece of land and sell it at a profit it is deemed to be income, and you pay income tax on it.

MR. COYNE: Suppose you sell it at a loss?

DR. PETRIE: But you are not in the real estate business, so you do not get a deduction of the loss.

MR. COYNE: If you run a grocery store and you have a loss you can deduct the business loss from the business income. I suppose it is a question of interpretation.

MR. LEACH: I think it is a problem of magnitude. If you make a loss on a capital transaction and the loss is so great that you have not the income to offset it -- to me, that is the problem; these things tend to come in great peaks and valleys, so that in the result you do not have anything to off-set.

THE CHAIRMAN: You have another four years in which to pick it up, though.

DR. PETRIE: Yes, but you have also the Department of National Revenue saying that it is not a business or trading loss. You have that additional thing to overcome.

THE CHAIRMAN: I am sorry; I thought you were putting this on the basis of its being a trading loss, but you are putting it on a basis of it being a contentious trading loss.

DR. PETRIE: Yes, different hazards are involved.

MR. COYNE: Yes, that is a hazard, I suppose, but it would be fair, I take it, to say that a business loss would be deductible from a business income even if the business loss happened to have arisen out of an adventure in the nature of trade.

Could we turn back then to an earlier part of your comments on the capital gains tax, to page 81 where in paragraph 146 you say:

> "The problem is serious in that there is no way of knowing in advance whether the results of a transaction will be considered a capital gain or taxable income. It may be really costly to a taxpayer who mistakes the difference between income and capital gains. The gain from a single transaction may be taxed at rates of 60 or 70 per cent or more. In view of the breadth of the statutory definition of income, the trend of its judicial interpretation and the increasing effort in assessment practice to follow the statutory concept of income, what is a tax-free capital gain today may well be taxable income tomorrow. This, briefly, is the heart of the problem, apart from theoretical considerations of

tax equity."

I wonder if it would be fair to say in this paragraph, and also in other paragraphs which follow, that your reasoning is directed primarily to the question of capital gains realized by individuals? Do the same considerations necessarily apply to capital gains realized by businesses? In other words, what are the principles which, in your view, argue against a capital gains tax to be imposed, say, on capital gains made by business as distinct from individuals?

MR. KEEPING: By corporations?

MR. COYNE: No, I would think it would have to be -- well, I put it to you simply on the general ground of business.

MR. LEACH: We think the same principles should apply, while admitting it is more difficult in that it is getting into the more contentious area. Profits or losses suffered by a business or a corporation are more likely to be related to the operation of the business. We stick to the fundamental principles that if you can define what is a true capital gain then it should still be free of tax for a business corporation as well as for an individual.

MR. COYNE: Let me put this to you, then; whereas in the case of an individual a capital gain may be purely fortuitous, in the case of a business frequently the costs of building up a capital asset are, in fact, deducted for tax purposes as operating costs during the year in which they are incurred, and yet if the asset, the value of which is built up

-26

in this way, is ultimately sold there is no tax on the gain. Is not that inconsistent with notions of equity and neutrality? This is a field with which I am not very familiar. There is, for instance, the development of good will through advertising and research expenditures, and, I suppose, the costs of developing a mining property, which is a special situation where capital costs are deductible for tax purposes.

MR. LEACH: Certainly you are introducing an area which is very difficult to comment upon. I certainly agree. On the other hand, what about a long term investment in land by a company as plant facilities, which land is eventually sold. That seems to me to be a true capital gain. Whether current expenditures are used in the development of a capital asset is a very difficult question. I would doubt that anybody could analyse that to a conclusion.

THE CHAIRMAN: We find some difficulty in this area. It has been argued in this area that all expenses of a business are deductible, and that you should have companies paying tax on a net worth basis. Is it rational really in Canada to say that we wanted to deduct all expenses of every kind, say only those with respect to land or securities, because the value continues there? Can we say that everything else ought to be deducted, and yet when we make a gain on the sale of our assets we are to apply the normal capital gains test as we do for individuals?

MR. LEACH: We would like to think that

more items be deducted -- that everything should be deducted unless they can be clearly indicated to a capital asset. I think our troubles have arisen because expenditures have been made which have been determined to be of an enduring benefit to the trade without developing any capital asset, or without any clear evidence that they were of an enduring benefit. What is "enduring"?

COMMISSIONER PERRY: There is one aspect of this that I do not recall whether you have touched on or not, and that is assuming that you do leave the situation just as it is do you think there are any grounds for alleviation of tax on a gain that is brought into income? I have in mind the fact that quite often these gains represent accruals over a considerable period of years, and in fact in any ordinary sense of income represent quite an unusual item of receipt. I do not know whether you have argued for any alleviation simply because of the unusual character of the income.

MR. LEACH: It is very nice to hear these questions raised because I have a note here on a piece of paper about them. Mr. Brown is also very interested in this, because we think the average spread of income of this type should be extended to this type of transaction, as is applied to individuals. In short, if a man is taxed on a real estate transaction he should at least have the benefit of averaging because the difficulty that he finds himself in is that of having to pay tax in one year on a progressive

rate. If he could be given a break like an author or maybe a hockey player, and so spread this or average it in some way then it would be of great help.

MR. COYNE: Does not that remove one of the principal objections that are expressed with respect to a capital gains tax as such? In other words, the fact that the capital gain may be realized in one year results in a very dramatic increase in income which would be taxed in that one year, and that could be made the subject of similar types of alleviating conditions to reduce or spread the impact.

MR. LEACH: What concerns us is the enormous administrative costs for the Crown and the taxpayer to say nothing about all the arguments of the changing value of the dollar, and also when this profit was really realized, and so on. As you say, it would certainly help if we could have some averaging.

COMMISSIONER PERRY: I think if you are applying our present concept of income it is immaterial whether it is a capital gain or not. It is income within a definition established by the jurisprudence. One has been guilty of carrying on a trade, in other words. But, it still emerges as a rather unusual kind of income, and income which may be sharply different from one's ordinary income.

MR. BROWN: That is why we think the individual should perhaps be given the same opportunity of averaging that as he is with other types of income.

THE CHAIRMAN: We have had several representations with regard to averaging for the individuals.

It has been proposed that it should be applicable on those occasions when an individual's income exceeds his average by more than a certain amount, which seems to be very equitable if it can be worked out.

In this area of capital gains, Mr. Leach, have you considered any alternatives such as a net worth tax? I do not know whether it is an alternative, but it is a tax which one might call a tax on capital. I know that a lot of countries which do not have a capital gains tax do tax on net worth. One economic benefit to be derived from it is, of course, that it is inclined to cause resources to seek out the most profitable uses so as to be able to get the return in order to be able to pay the tax.

MR. LEACH: We have not considered it seriously, Mr. Chairman.

THE CHAIRMAN: Quite a number of the large European countries have that.

COMMISSIONER PERRY: I think we should say, Mr. Coyne, it is certainly the best balanced presentation on the pros and cons for a capital gains tax that we have had in any brief.

MR. COYNE: It is very helpful indeed, Mr. Chairman. I have not many points into which I can probe. I have one other question in this section. It is really a small point, and it arises out of paragraph 162 which commences at the bottom of page 91. You are dealing here with the case for taxing capital gains, -- the various arguments that

are put forward in this connection -- and specifically under the heading of "Tax equity" you say:

> "Another point connected with tax equity is that a preferential tax treatment of capital gains concentrates the benefits in the hands of upper income bracket taxpayers with the greatest tax-paying ability. Yet when the alleged (and perhaps real) inequity of preferential tax treatment of capital gains is laid beside the inequity of taxing them as ordinary income at steeply progressive rates (not to mention the economic consequences of such policy), the policy makers are faced with a Hobson's choice."

That is, a Hobson's choice as between the two degrees of inequity.

Could it be suggested that the greatest inequity of all is not to tax them at all, which is what we do if we are thinking strictly in terms of tax equity?

DR. PETRIE: Well, I think we have tried to cover it, Mr. Coyne?

MR. COYNE: We are talking here of equity, though. I think your ultimate conclusion against a capital gains tax, when you have boiled down all these arguments which you have considered pro and con, is that there appears to be very little revenue

A-31

to be derived from an exceedingly complex and expensive administration.

MR. BROWN: And that there is very little of that capital gain which is not caught through the established taxes eventually.

MR. COYNE: Yes, I take that point as well. Of course, these arguments are put before us by others and they have to be considered, and in particular there is this question of tax equity. I am dealing purely with that aspect of it. Is there any answer to the suggestion that the greatest inequity of all between these choices, whether they are to be made by Hobson or someone else, is not to tax capital gains at all?

MR. LEACH: The changing value of the dollar would be a perfect answer. If there was, in fact, no real gain, and the gain expressed in terms of dollars arose only in terms of the changing value of the dollar, then it is not proper to tax it.

THE CHAIRMAN: I do not think that is the answer Mr. Coyne is reaching for. May I, Mr. Coyne?

MR. COYNE: Certainly, Mr. Chairman.

THE CHAIRMAN: One inequity -- perhaps you will persuade me that it is not an inequity at all -- is the fact that shareholders of a public company can sell their shares after a number of years at a gain without tax. There are two streams of income for them. One is the distribution of dividends

upon which they pay tax, and the other is cumulative. The part that is cumulative bears only a corporation tax, whereas that which is distributed pays two taxes; it bears the corporation tax as well as the shareholders value of the stock upon which he can realize without paying further tax. You have, I think, made reference to that in your submission by saying that there is an imbalance there, but I would have thought that that is also an inequity in the capital gains tax.

MR. LEACH: If I could argue for a little bit on a technical point, I do not think it is the accumulation of earnings which reflects itself in the price of the stock.

THE CHAIRMAN: Mr. Leach, taken over a ten-year period ---

MR. LEACH: I suggest that the price of the stock is determined by the growth of the annual return -- the return on the market price, if you like. I think we all agree that the book value of a company's stock, or a shareholder's equity in the company, is not the true value of it on the market. Things such as present earnings and the prospects of future earnings affect its price, and I do not think you can reflect the increase in market price in the ---

THE CHAIRMAN: Neither can I analyze it over a long period of time. I do not think there is much doubt but that over a period of time during which I might hold a share -- let us make it ten years -- it certainly appreciates, and that the value

of the share is not entirely unrelated to the accumulation of income there. The income has swollen the capital, and the capital has gone to work and earned more money. The earnings have increased because the capital has been put to work. As long as that occurs there is an appreciation in the value of the shares -- that is, as a result of this plowing back.

MR. LEACH: I will certainly agree that it is not entirely unrelated.

THE CHAIRMAN: If you wanted to stop at that point then that is fair enough.

COMMISSIONER PERRY: I wonder if Dr. Petrie would tell us what the accepted creed is amongst the security analysts.

DR. PETRIE: Creed in which way, Mr. Perry?

COMMISSIONER PERRY: As to what factors affect the value of a stock, the earnings distributed or the earnings undistributed?

DR. PETRIE: This may sound almost facitious, but I do not mean it at all in that way. I think it is basically in terms of how many people want to sell in relation to how many people want to buy. I can give you a classic example of what happened in the last six or seven months to one security, namely, U.S. Smelters. This had nothing to do with earnings and nothing to do with net worth, book value, or anything else. A group of Americans decided to take over the company. They decided to acquire control, and they bid the shares up from $50 odd to over $100.

The stock was trading yesterday, I think, at $97 or something like that. That had nothing to do with anything except how many people wanted to buy in relation to how many people wanted to sell. I think it is as simple as that.

COMMISSIONER PERRY: The securities market is no more predictable than any other market.

DR. PETRIE: This is true. It is less predictable than the market for base metals because at least in base metals or other commodities you have some clue as to the industrial demand for such commodities, but you have no clue as to the stock market demand for a particular stock in a particular company. You just do not know, and it is the sort of thing that goes on all the time.

MR. LEACH: I would like to disagree mildly with my colleague on this issue. I have seen shares underwritten -- we all know what happens when a company comes on to the market for the first time. The underwriters set out the pattern of comparable securities. They find that these securities are selling for "X" times the earnings, and that there is a certain dividend pay-out according to the custom of that particular industry and the market in general, so the underwriter says: "This stock will sell at 17, and you should put it on at 75". There is an interrelationship between these factors, and it is on this basis that the underwriters take the issue and sell it at 17.

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18

THE CHAIRMAN: I am in the happy position of agreeing with both of you. I can quite agree with what Dr. Petrie says and I can quite agree with what you say; but there are certain things having to do with higher income -- the price ratios of earnings seem to follow a pattern. Good companies seem to be different from poor companies over a period of time; they move up and down and so the market moves up and down, but you have generally got some idea of the worth of most of these things.

We have had the investment dealers before us and they believe that it gives average yield. It seems to make sense. But I quite agree that from day to day all those things can happen. I am talking about accumulation of earnings. I am thinking of the long range effect; and if it is an even better company ten years from now than it is today the company's earnings will go up and they will have some reference to...

DR. PETRIE: At the same time the market may pay no heed to it.

Several years ago I worked out some rather amusing figures; but let us go back about five or six years. Take International Nickel at the peak of the 1929 bull market. If you had held it through from 1929 at what you bought it for at the peak you would have been out of pocket. If you had bought Aluminum Limited you would have made 25 or 30 times your original investment. In other words, over the

long pull the market just didn't pay any attention to International Nickel as compared with Aluminum, for one reason or another.

This is all I am saying, that I don't pay any attention to the stock market at all in terms of evaluating a company.

MR. COYNE: That brings me to the end of the Capital Gains section which is at page 96.

You, Mr. Chairman, or your colleagues may want to ask some questions on some of the intervening pages.

THE CHAIRMAN: You have more on sales tax, Mr. Coyne?

MR. COYNE: Yes, Mr. Chairman.

THE CHAIRMAN: Then, let us get on with the sales tax, Mr. Coyne.

MR. COYNE: Well, then, I would like to turn over a number of pages to page 105. You are dealing here with the general subject of "approaches to sales tax in Canada," and the number 2 you caption "Designated Sale Price," which is the approach that was put forward by the Canadian Tax Foundation some uears ago to the Sales Tax Committee. You say:

"If it is impossible to find an equitable national sales price..." -- should that be "notional"?

DR. PETRIE: "Notional" is right.

MR. COYNE: "If it is impossible to find an equitable notional sales price, another alternative exists, the principle of

adjusting selling prices to remove the extra costs incurred by a manufacturer in performing distributors' operations..."

Now, I note that you simply are describing an alternative system of tax and not taking any position or making any specific recommendations, and perhaps the proper answer to the question I asked is to go out and look at the Canadian Tax Foundation representations; but I wonder if you would explain a little of what is in mind here and how such a procedure could be administered from a practical point of view?

DR. PETRIE: Well, as we have spelled it out the problem is tricky. I don't profess to be sophisticated, but I realize the nature of the problem and the fact that the manufacturers' tax, as now imposed, has certain major difficulties which have been point out to the Commissioners.

Beyond that I am afraid I haven't any constructive comments, Mr. Coyne.

MR. COYNE: Right. Well, then, you deal rather briefly with the sales tax and express some general recommendations as to what should be done with it. Your principal recommendation -- and I am referring to page 13 of the preface, although I think it also is cited later on when you come to your conclusions -- you recommend that "...a broadening of the salestax base be effected and possibly in the 'services performed' area."

DR. PETRIE: Right.

MR. COYNE: And in paragraph 184 on

page 106 you say:

"There are many refinements of the basic problem of any sales tax, the tax base..."

I wonder if you could elaborate a little on what you feel are the possibilities of broadening the tax base in the sales tax area?

DR. PETRIE: Well, I think this can be rather briefly and simply expressed, Mr. Coyne.

We have in mind including certain areas of service in the sales tax which are now exempt, which could be substantial producers of revenue.

For example, we all remember, I think, that during the war, for instance, the triple sales tax was applicable to electric energy, which we in our submission consider only one area. Our thought was, without being specific, that you could take in a great number of different types of service which pay no tax, which are not commodities and which are exempt -- bring them into the fundamental base of the whole tax structure -- to compensate for the lowering of personal income tax and corporation tax. We have suggested this to pick up the loss in revenue from our proposals, and we feel that with this proposal you would pick up the revenue lost assuming that the best you can hope for is at least a retention of something like the present revenue level.

Therefore, we are arguing only that there is a broad area of service performed which could be brought into the tax base.

MR. COYNE: It is sometimes put to us, Dr. Petrie, -- and of course many people have made the same general recommendation that you do -- it is sometimes put to us that the only practical way in which service could be taxed over a sufficiently broad base would be to convert the federal tax to the retail level and in effect deal with the provincial and federal taxes in the same way.

It has even been suggested that it would be only at the retail level that sales tax on service would be an effective source of revenue -- would cover a sufficiently broad field. Do you agree with that?

DR. PETRIE: No, I don't think that it is the simple fact that it has to be at the retail level. There are pros and cons, and among the cons are the administrative problems.

THE CHAIRMAN: No; it was service that Mr. Coyne referred to. Would you tax services at any other level than retail?

DR. PETRIE: Yes, I think so.

THE CHAIRMAN: You have cut off, I would say, half a billion dollars at the moment.

DR. PETRIE: Roughly.

THE CHAIRMAN: And to catch up with this half billion dollars it looks like about four and a half billion in a broadened base on sales and service?

DR. PETRIE: Not that much. If you take the incentive -- the cost incentives -- and I am referring to the June 13 budget -- we see one hundred million there, and we see many of those

exemptions; and we say tax cooperatives as all other companies are taxed.

THE CHAIRMAN: Have you got a rough idea of how much it would produce?

DR. PETRIE: There are the credit unions. This will get you 20 or 25 million; we are not quite certain. Maybe it would be smaller than what you suggested -- in the neighbourhood of half a billion -- for service.

THE CHAIRMAN: Knock it down -- 350 million.

DR. PETRIE: I have made a rough calculation. Say 350 million.

THE CHAIRMAN: With a 4 billion base to get to; and, of course, we go to the retail...

DR. PETRIE: 3 billion 2.

THE CHAIRMAN: You are quite right; and if we went to the retail level, because we can't tax haircuts and laundry and so on, you would have to bring the rate down.

DR. PETRIE: There is another way of doing it and that is to have excise taxes at this level; and this is the Chamber's view.

THE CHAIRMAN: It doesn't broaden the base.

DR. PETRIE: It does broaden the base in this way, that you are not going to bring it into taxable income but you are going to bring into the tax structure certain things tax free at the moment at the consumers' level, not at the producers' level.

If you don't like the idea of trying to apply manufacturers' sales tax to barber shop service and laundry service and services in general then there is another alternative and that is that you could have a special excise tax.

COMMISSIONER WALLS: You would have to have a remarkable amount of it; and without going into the full broad concept of services you are not prepared to recommend -- or we may have had some figures for some things that you mentioned, such as barber shops, laundries, dry cleaing, photo studios, and if we did tax them the tax ratio would be in the neighbourhood of 39 or 40 million.

DR. PETRIE: I don't think you mentioned the really important one.

COMMISSIONER WALLS: That is what I am anxious to hear.

DR. PETRIE: Supposing you take fuel -- consumers' expenditure on fuel. This is not industrial; according to the national accounts, 440 million dollars; and consumers' expenditures on electricity, 345 million; on gas 137 million; on telephones 353 million; on transportation -- this is not on company accounts -- 434 million. You can go through the national accounts and you can add up all the many billions you want on these services. We are not recommending what services should be singled out for taxation.

THE CHAIRMAN: What would these you have given add up to?

DR. PETRIE: A billion nine.

THE CHAIRMAN: And you would not suggest that this would be subject to the 11% tax, because this tax would be at the retail level? The present sales tax probably affects consumers at 6 or 7%?

DR. PETRIE: About that -- perhaps 8%.

THE CHAIRMAN: So that the tax would have to come down to some such level as that, would it not?

DR. PETRIE: Well, again, Mr. Chairman, we are as a group not advocating a retail sales tax. This is not the Chamber's policy. We are merely expressing the view that to broaden the tax base you can tax certain services that are not now taxed.

THE CHAIRMAN: I think we are puzzled as to how to go at those services except at the retail level.

COMMISSIONER PERRY: I think the problem is that these are all services rendered for the final consumer; they are not services rendered by the manufacturer.

DR. PETRIE: That is right.

COMMISSIONER PERRY: Therefore by definition you are at the retail level?

DR. PETRIE: Except that there is precedent, remember, because the sales tax during the War was eight per cent and it was on our Hydro bills in the city in which I live.

COMMISSIONER WALLS: You realize that there are a number of utilities which are already taxing the power and including sales tax in their bills. Also telephone bills include sales tax. The amount charged is five per cent. So if you add another eight per cent, you would be taxing these power bills by 13 per cent. Do you think there would be much of an uproar from the consumers. Of course, you would be giving them the benefit of seeing this tax visually, which they are all so anxious to do. They would see what is being done by the government. But how happy would the taxpayer be if there were a 13 per cent tax?

DR. PETRIE: It might not be a bad idea to let the taxpayer know what is the cost of government.

COMMISSIONER PERRY: I think we get the point that you are trying to keep at the level of this type of consumer service and not get back into industrial transportation and things which enter into industrial costs.

DR. PETRIE: That is the point. We do not want it at the retail level if it can be avoided.

THE CHAIRMAN: You are not suggesting this as a good subject for taxation, are you? I do not mean on the producer, but on the consumer.

DR. PETRIE: Frankly, Mr. Chairman, I had not thought about it.

THE CHAIRMAN: It is a good sized base and it is taxed in other countries.

DR. PETRIE: That is right.

THE CHAIRMAN: Your general recommendation here does not refer to the level at which the tax is to be applied, which leads us to believe that you are recommending no change in the manufacturers' level.

DR. PETRIE: That is correct.

THE CHAIRMAN: So I deduce from that that you concluded there is not a better level on which to assess the tax than the manufacturers' level?

DR. PETRIE: This is our view.

COMMISSIONER WALLS: With regard to that, did you compare it with the other possible levels of taxation, or was this just the majority opinion of your membership already, that they liked the

manufacturers' tax?

DR. PETRIE: This is the opinion of our membership, sir.

COMMISSIONER WALLS: Thank you.

THE CHAIRMAN: I do not think we have any more questions on sales tax, Mr. Coyne. Do we need to get into Provincial and Municipal taxes?

MR. COYNE: I was not proposing to do so, Mr. Chairman.

THE CHAIRMAN: We could move to estate taxes, then, which is on page 109.

MR. COYNE: Yes. I would like to turn to the following page, 110, where you make the statement, in the middle of paragraph 194:

> "Federal death duties in Canada are basically an adjunct, along with the gift tax, to personal income tax as a measure to protect the revenue from tax evasion".

This is a rather startling statement, to me, not because it suggests that one of the purposes served by death duties is, in a sense, to police the income tax returns the man has filed during his lifetime, but I would have thought that the tax is supported in principle on the view that it is desirable to prevent undue and permanent accumulations of wealth that can be passed on from one generation to another; and the estate tax, certainly the Federal estate tax, is deliberately designed to cut down on accumulations at the time of death. That was indeed the principal purpose of the tax. Do you have a

different view?

DR. PETRIE: I do. I took the trouble to look at the Budget Speech of the Minister of Finance when he introduced this measure during the War.

MR. COYNE: You are speaking now of 1941?

DR. PETRIE: That is right. This was the expressed view of the Minister.--

MR. COYNE: I suppose that when the tax was introduced in 1941, as indeed when the Provincial succession duties were first introduced in the 1890's, they were essentially revenue measures?

DR. PETRIE: That is right. But the Federal tax was not introduced as a revenue measure.

MR. COYNE: It was not?

DR. PETRIE: No.

MR. COYNE: Perhaps you would describe what your research into the Budget Speech of 1941 indicated.

DR. PETRIE: The Minister said very little by way of rationalization. He gave warning in advance that this might not be considered as a temporary, wartime measure but might be a continuing measure.

I think most of us in this room have been around long enough to know some of the arguments, in private at least -- not in public in the House of Commons -- that were given to support the measure. It is a policing measure. This is my firm conviction,

Mr. Coyne:

MR. COYNE: Is this how it should be regarded? In other words, is that the only basis in the Chamber's view as to how an estate tax can be justified?

Whatever may have been said concerning the original purpose, can it now be said that death duties are justified in terms of the social purpose, if you like, as I suggested a moment ago?

DR. PETRIE: I cannot speak for the Chamber. I would prefer to have Mr. Brown or Mr. Leach speak on this, because my views are not entirely four-square with Chamber policy on this matter.

MR. BROWN: We know that the purpose of the estate tax was as Dr. Petrie said it was. We know that there have been some difficulties in its application, and we have taken the stand, as a Chamber that we have not asked for its repeal as such; but we have asked for the amelioration of its application to avoid the double taxation that occurs between it and income tax and to provide for a clearer situation in respect to instalment payments, assets, and so on.

These are areas in the administration of the estate tax that we have had a long-standing policy on, that we have taken up time after time, looking towards a better, a fairer application of the estate tax as such.

MR. COYNE: Within the confines of the present legislation, by and large?

MR. BROWN: That is right. As we say in this brief, it has not an important yield as far as the income of the Federal Government is concerned; it is something like 1.3 per cent, I think we mention here in paragraph 194.

There has been a question as to whether it should be here in the hands of the provinces, and we come back again to what you raised this morning, Mr. Walls, about where things fit.

However, our attitude is that as it stands we are not asking for its repeal, but we are asking for amelioration in some areas with regard to its application.

MR. COYNE: Thank you very much.

MR. KENT: In elaboration, Mr. Coyne, of what the President of the Executive Council has said, particularly the Chamber seeks the removal of inequity which capitalizes pension payable to widows without even taking into cognizance the income tax features of those pensions, and the redress of certain grievances concerning the recognition of charitable trusts and the rate of encroachment. But these are all administrative matters.

The fundamental view as expressed here is that it does play a useful part in a rounded tax structure, and as such we do not seek its repeal.

MR. LEACH: I do not think Mr. Coyne's original question has yet been answered.

MR. COYNE: I will revert to Dr. Petrie, if I may, for a moment.

COMMISSIONER PERRY: I want to go back to this business of the origin of the tax. Is that what you are going on with, Mr. Coyne?

MR. COYNE: Yes. I was going to suggest to Dr. Petrie that there would be no justification at all for charging the tax purely for policing purposes. In other words, surely if the only purpose of the tax was a policing one, then the feature which involves the policing is the filing of returns and the disclosure of information, and this could be called for by appropriate legislation without imposing any tax.

MR. LEACH: My comment would follow that I think we must, as individuals, admit that this has had some success in perhaps preventing the undue accumulation of inherited wealth. Whether that is a good thing or not is another question.

COMMISSIONER PERRY: The actual situation was that the 1940 budget was delivered following the collapse of several conferences to consider the recommendations of the Rowell-Sirois Report, and it made an effort to salvage as much as could be salvaged from those recommendations.

One of the recommendations was that the Federal Government not only impose a death duty tax, but take over the field entirely. There were other things in the budget which were in the same vein. So I do not think it is entirely true to say that it was just an administrative device.

MR. KENT: I do not think we rest it

entirely on that; but, as I said before, it does form part of a well rounded tax structure. I do not think Chamber policy really goes much beyond that.

THE CHAIRMAN: Time is marching on, and we said we would finish by 4 o'clock. Is there anything more on this section, Mr. Coyne?

Perhaps the most significant matter that is left is the recommendation with regard to incentives.

MR. COYNE: Yes, Mr. Chairman. I must say that I just have one or two questions to ask on this question, which starts at page 119. I think perhaps it is true to say that the Chamber's position on the question of incentives is a rather general one which perhaps was expressed quite clearly this morning; the general preference for tax neutrality as against discriminatory incentives.

With regard to the various incentives which you have described as being now factors in our tax structure, you refer to depreciation at the bottom of page 120 and then over onto page 121, where you describe the capital cost allowance system. You say:

> "This is the principle at present operative under the Income Tax Act. No particular incentive is attached to the plan".

Would it not be fair to say that the capital cost allowance system in practice indeed represents a system of accelerated depreciation, and to that extent is an incentive system?

DR. PETRIE: To the extent that it is

accelerated over and above normal accounting practice I suppose there is this incentive.

THE CHAIRMAN: That is to a very large extent, if one looks at a couple of balance sheets and adds up the reserves on them. I have the addition here of some company balance sheets and I was quite struck with the amount. It is in hundreds of millions of dollars.

MR. COYNE: I think there is information on hand before the Commission about that.

THE CHAIRMAN: I cannot find it at the moment. It is a very large figure.

MR. COYNE: In fact, I suppose in general principle one could argue that as far as tax neutrality is concerned one might have to have serious doubts about the capital cost allowance system as compared with an accounting system, if you like?

MR. HAMILTON: Except that it applies to all companies. It is not selective of one company or one area; it applies to all companies subject to the corporation income tax.

MR. COYNE: I suppose that is true, but surely it assists the capital-intensive industries to a far greater degree than it does labour-intensive industries which derive no benefit at all?

MR. HAMILTON: It is a short term benefit.

MR. LEACH: The industries which have large capital investmentshave laid their money out.

THE CHAIRMAN: Mr. Leach, we are looking at an approximation of about $1 billion. That is an approximation of the amount which the government would have received if taxes had been levied based on depreciation which appears in the company's books, which is obviously the fairest measurement of income and which the managers report to the owners. Taxation has permitted a higher charge than the fairest measure of income, and to that extent there has been $1 billion approximately -- subject to the accuracy of this figure which I am not prepared to stand behind -- less paid into the government than otherwise would have been the case, and no interest would be paid on the $1 billion. So that to the extent the government is out, there is an annual cost to the government of the interest on $1 billion, whatever that is, and an annual benefit to the company of the amount of that interest.

MR. LEACH: Mr. Hamilton said that we preferred not to think of that as a kind of incentive but as something available to every business entity, incorporated or otherwise. It may well

be a stimulus to business activity, and we certainly think it is in the interests of the country. But it is not discriminatory. It is available to everyone who puts out their money to buy capital assets.

THE CHAIRMAN: It is available to anyone who invests in capital assets. Some people in business do not.

MR.KENT: With respect to your point that it is costing the country whatever is the interest on $1 billion, Mr. Chairman, I think that is a highly notional amount because it merely means that the government has deferred whatever collection may fall on that amount. It is a government measure which has equally assisted all persons and corporations who are required to find the capital to carry on their business.

THE CHAIRMAN: I think we are together on that but not on the point where it is a notional amount. The government would have had $1 billion which it still has not got were it not for this system.

MR. KENT: It is hard to translate that because it has been forgone at this time as a cost. It is merely a matter of timing of the write-off, as we know.

MR. LEACH: On the theory you expressed earlier in connection with the accumulation of earnings, that money has been reinvested to produce more income, which in turn is taxed. So perhaps this is where Mr. Kent considers that it is notional.

COMMISSIONER GRANT: It is reinvested all the time. It is designed to take care of what is the lifetime of a given asset.

THE CHAIRMAN: That means that it is better invested by industry than by the government. It is better invested in profit-making investments. I think the government expenditure is excellent expenditure, and I think that you gentlemen must agree with that.

MR. LEACH: I did not say better invested. What I said was invested in such a way as to produce taxable income.

THE CHAIRMAN: If the government invests it, I suggest that that also increases the income of the people and reduces their taxable income. I think you must agree with that. Am I right, doctor?

DR. PETRIE: Yes, Mr. Chairman, I agree except for one point. I am not satisfied that the government choice of investment is as good as, or better than, that of ---

THE CHAIRMAN: No, I did not say it was better.

MR. BROWN: Even with the operation of this system, such things as tools in the type of Canadian industry referred to have an average age of 7.7 years. Obsolescence is approaching. Obsolescence is approaching, and we also have to find new jobs for 150,000 people, increasing the work force each year. If we are to do that, we

will have to have a great deal of support for the industrial fabric of the country in order to compete in world markets, which requires the use of capital to perform or secure adequate up-to-date effective equipment.

THE CHAIRMAN: I have no quarrel with that at all. Could you, Mr. Brown, give us some information with regard to the average age of equipment? I have asked our staff to find where there is a suitable survey so as to secure this information. As far as I have discovered there are no current Canadian surveys. There is an American organization which, I think, takes a census of equipment every so often.

MR. BROWN: If my memory serves me aright, I think the figure which I quoted was given during a conference of a group of economists which met under the aegis of the National Investors Conference in Montreal late last month. However, I will be glad to check that, and if I can substantiate that information I will be glad to send it on.

THE CHAIRMAN: I should like to know whether our notional equipment is getting older or younger.

MR. BROWN: The information that I have is that it is getting older, and that it is a really serious problem.

THE CHAIRMAN: We would very much like to know all about it.

MR. BROWN: I suggested that that might indicate whether this is being really effective.

THE CHAIRMAN: I agree.

MR. COYNE: I was not proposing any further questions on the incentive section, Mr. Chairman. However, I do have a place marked at the very end of the conclusions, on pages 136 and 137.

MR. BROWN: Before we reach that, I should like to draw to your attention what we say on page 127, at the end of paragraph 232. This is in connection with the question of the tax-free status of provincially-owned power companies, and so on. We believe that that has led to certain actions in this country which have not been viewed with complete calm, shall I say, within our circles.

THE CHAIRMAN: Well, have you an answer for that? I did not see one in here.

MR. BROWN: We suggested that we do not like a special category in this regard. We say:

> " Special forms of corporate enterprise have been accorded either total exemption from tax or special tax status."

This is a general section and it is included in there.

MR. COYNE: In effect, you indicate the view that there is no reason why provincially-owned power companies should not pay taxes in the same way as many other Federal Crown corporations pay taxes.

MR. BROWN: That is correct.

COMMISSIONER WALLS: You mean that each type of government should charge the other the taxes which they normally charge to other individuals?

MR. BROWN: If the Federal Crown corporations are considered as taxable entities within the realm of Canada, then presumably provincial charter companies or provincially-owned companies should too. At least, this is our thinking.

COMMISSIONER WALLS: And the municipalities should charge the provincial government property taxes, and so on?

MR. BROWN: This is tax neutrality.

THE CHAIRMAN: I have no trouble with that at all. It seems that proper accounting would require that that should be done. But I do have the greatest difficulty in seeing how in practice it could be achieved under our law.

MR. BROWN: There are two attitudes to this. One is to remove Federal tax from the privately owned if you cannot tax the other. In other words, put them in the same bracket.

COMMISSIONER WALLS: Then you create inequity between that branch of industry and other branches. That is the trouble with that kind of action.

MR. BROWN: I grant that, but we have a different course, Mr. Walls. It is a question again of Hobson's choice.

MR. LEACH: Let us not overlook that the

private utility is subject to rate income.

THE CHAIRMAN: The privately owned utilities, as you know, have recommended to us that corporation tax be replaced by some kind of sales tax on their products.

MR. BROWN: Presumably that would apply to publicly owned utilities as well.

MR. COYNE: There is just one small question that I overlooked on another subject, and I wonder if I could take it up very briefly. It has to do with personal income taxes, and I am looking at page xi of the Introduction, where you have a summary. You say immediately about the paragraph containing the recommendation:

> "A lower tax applied to a broader tax base would produce as much revenue with fewer adverse economic consequences."

I am just not clear on that. You are not suggesting that the personal income tax base can be broadened and a lower rate applied to produce the same kind of revenue from personal income tax?

DR. PETRIE: No. What we are suggesting here is a profit tax base including lower service tax under sales tax.

COMMISSIONER PERRY: Well, we are now at our deadline, but I do want to make one general comment on the proposition of more indirect taxes and less direct taxes.

It has been pointed out by serious minded economists -- and I certainly do not except

any of those present under that classification -- that the Canadian corporate price structure is fairly rigid; that it could very well happen that if corporation profits taxes were reduced, that would have very little effect on corporate prices. It would have very little effect on the price of goods sold by corporations.

Then if one added to the price of goods sold an indirect tax, one could easily end up with a generally higher priced structure than now prevails, with resulting problems of international competition, higher wage demands, and all the rest of it. In other words, if you are thinking of transfers of aggregate amounts of tax burden from one area to another, unless you get compensating price changes in those areas you could easily distort your prices and your competitive export position, of which we are all very conscious, to the extent that your changes do not exactly offset the other difficulties. Perhaps the order of change suggested here might not be significant, but people have been suggesting more drastic changes and removing corporation profits tax, unloading it all on to indirect taxation. I think some of the danger is inherent in your proposals.

DR. PETRIE: I think that all we can say to that is that this is a calculated gamble, Mr. Perry.

COMMISSIONER PERRY: I am afraid that nearly everything which we have heard indicates that

it is not so much of a gamble. We have had manufacturers telling us that it would be very unlikely that there would be any immediate change in their prices, even if this manufacturers' sales tax was taken off. When you get manufacturers making statements of that sort, you really begin to wonder what it is which would change our price structure.

MR. LEACH: I do not know whether it is clear in the brief, but in private conversations which we have had we have emphasized to each other that we do not want an extra tax burden on production, which is our responsibility.

COMMISSIONER PERRY: In the eyes of an economist it is very hard to have taxes which will not be on production. Make these things as remote from the productive process as you will; all you have to do is to affect the cost of living index and this will affect wage demands and costs. Therefore it is hard to escape.

This has been a little sermon, I know, so I will leave it now. But I do think this idea has been a little too glibly accepted that you can short circuit some of the factors involved.

MR. LEACH: I should like to ask Mr. Kent to say a word or two on the subject of the pre-budget submission.

MR. KENT: Mr. Chairman, we have filed with you the submission made last year to the responsible ministers. It has been the policy

of the Chamber year after year to repeat various areas of the taxing statutes on which it recommends that action be taken. This year the Chamber revised its policy and took cognizance of the fact that your Commission was sitting, and that there was very little chance that the government would attack any of the major areas until such time as they had had the advantage of your deliberations.

Very shortly the Chamber will again be publishing its pre-budget brief to the responsible minister, and they have limited their recommendations this time to the various matters that there is some possibility that there could be immediate action on, and did not dwell upon the field of far-reaching policy about such things as service distribution or the benefits of capital cost allowances and other matters of that kind; and we have done our best to use the pre-budget brief of 1964 as a hinge between those matters of Chamber policy that previously have been expressed and the basic matters of policy that we have put before you; so that even although you might examine last year's brief and the brief submitted to you and came to the conclusion that there were certain anomalies and contradictions in the comparison we would ask you to withhold judgment on us until you have seen our pre-budget submission for this year.

That is all I have to say on that point.

THE CHAIRMAN: Please send it to us.

Is there anything further you would like to say?

MR. BROWN: I would like to thank the members of the Commission, on behalf of the Canadian Chamber of Commerce, for being with us today. We appreciate your courtesy and the way you have joined with us in the discussion of these problems, and particularly we appreciate your devoting your Saturday and perhaps foregoing a visit home for some of you for the week end.

I might point out in passing that it is, in fact, those of your own profession who have afforded the time to come before you, as you will perhaps recognize that our delegates have been made up of your own chosen profession; but we thought that in order to give you a well-versed presentation and to discuss this question of taxes we either had to go to the legal profession or to our chartered accountants, and since you spent last Saturday with the legal profession we thought it would be desirable that you should spend this Saturday with us.

Seriously, our tax structure is complex and change creates problems, and we propose to use much of the material we have included in the brief we submitted to you as an aid to the better understanding by Canadians, and, more particularly, by our own members, of the whole tax picture in Canada. I think you will agree that such a program of educational effort by us might be in the long term interest of all Canadians.

THE CHAIRMAN: Thank you so much, Mr. Brown. We recognize that certainly this is not an easy subject at all, as we go on; the complexities are immense; but what you have given us today is a tremendously good submission which will not only be helpful to the commissioners but will assist our staff. It is a profound document.

I am particularly grateful for your use of the questionnaire to your members, and I read the answers with a great deal of interest. I see that you have used them in the document and if we had a little

more time we might have commented on these replies and examined them more carefully. But, as I say, it will not only be useful to us but it will be useful to our staff.

Thank you very much indeed for giving your time and your effort to the preparation of this and for coming to see us today. It was quite an imposition on you. What you have done has been of immense value to us in this job we have undertaken.

Thank you very much, gentlemen.

We will stand over till 9.30 a.m. Monday.

--- Adjournment.

ROYAL COMMISSION

ON

TAXATION

HEARINGS

HELD AT

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ROYAL COMMISSION ON TAXATION

Proceedings of hearing held before the Royal Commission on Taxation in Supreme Court of Canada Building, Ottawa, Ontario, commencing at 9.30 a.m. on Monday, January 20, 1964.

THE COMMISSION

Mr. Kenneth LeM. Carter, Chairman.
Mr. J. Harvey Perry
Mr. A. Emile Beauvais
Mr. Donald G. Grant
Mrs. S. M. Milne
Mr. Charles E.S. Walls

LEGAL ADVISERS: Mr. J. L. Stewart, Q.C.
Mr. J. Coyne

RESEARCH DIRECTOR:

Prof. D. G. Hartle

SECRETARY:

Mr. G. L. Bennett

INDEX TO EXHIBITS

* * * * *

SUBMISSION OF

THE CANADIAN BANKERS' ASSOCIATION

APPEARANCES

Mr. W. M. Currie	Chief General Manager, Canadian Imperial Bank of Commerce
Mr. Leo Lavoie	General Manager, The Provincial Bank of Canada
Mr. H. L. Robson	(Secretary)
Mr. D. G. Keaveney C.A.	Controller Canadian Imperial Bank of Commerce
Mr. M. H. Maltby	Assistant Chief Accountant, Canadian Imperial Bank of Commerce
Mr. T. A. Boyles	General Manager, The Bank of Nova Scotia
Mr. M. G. Clennett	Supervisor of Organization, The Royal Bank of Canada
Mr. M. A. Crowe	Economic Adviser, Canadian Imperial Bank of Commerce
Mr. L. P. Deschenes	Superintendent, Banque Canadienne Nationale
Mr. J. Machabee, C.A.	Assistant General Manager, The Provincial Bank of Canada
Mr. R. E. Saunders, F.C.A.	Chief Accountant, The Toronto-Dominion Bank

THE CHAIRMAN: Mr. Secretary, are you ready?

THE SECRETARY: Yes, Mr. Chairman.

Mr. Chairman and Commissioners, the first submission on this, our last week of public hearings, is to be presented by the Canadian Bankers' Association. Mr. W. M. Currie, President of the Association and Chief General Manager of the Canadian Imperial Bank of Commerce is here together with a number of his associates. Mr. Currie would like to make a few introductory remarks and introduce his colleagues.

I would like to enter this brief into the record as Exhibit 326.

--- EXHIBIT NO. 326: Brief of the Canadian Bankers' Association.

THE CHAIRMAN: Thank you. Good morning Mr. Currie and gentlemen. We are very glad to see you. It is nice of you to come and assist us today. We appreciate what you have already submitted before us which we have read with considerable interest. I am sure as we go on we will have a few questions to put to you. We have asked our counsel, Mr. Coyne, to lead the questions. It may be more sensible, of course, to ask Mr. Perry to do that. He said he would not. Mr. Currie, I believe you wish to make some remarks?

MR. CURRIE: Very briefly, Mr. Carter.

I should perhaps say how glad we are to be here and how interested our Association is at the importance of the work of this Royal Commission and what effects it will have on the economy. You have read our brief and you are familiar with the features we have there tried to develop. These are the concern of the Chartered Banks, and I may say Mr. Keaveney and his group have prepared the brief very carefully.

The Association hopes that it will add to the work of your Commission in its deliberations.

I would like to introduce the members of our party. Mr. L. Lavoie, Vice-President of the

Association and General Manager of the Provincial Bank of Canada. Mr. H. L. Robson, Canadian Bankers' Association, who I am sure is known to all of you. On my right Mr. D. G. Keaveney, Comptroller of the Canadian Imperial Bank of Commerce and Chairman of the Canadian Bankers' Association Committee. Mr. M. H. Maltby , at the end of the table, Assistant Chief Accountant, Canadian Imperial Bank of Commerce and who acts as Secretary of our Committee. Mr. T. A. Boyles, General Manager of the Bank of Nova Scotia. Mr. M. G. Clemmett, Supervisor of Organization of the Royal Bank of Canada. Mr. M. A. Crowe, Economic Adviser, Canadian Imperial Bank of Commerce. Mr. L. P. Deschenes, Superintendent, Banque Canadianne Nationale. Mr. J. Machabee, Assistant General Manager, The Provincial Bank of Canada, and Mr. R. F. Saunders, Chief Accountant of the Toronto Dominion Bank.

In responding to the questions which the Commission will wish to direct to us, we propose that Mr. Keaveney and members of his group will deal with those questions which call for exact and detailed answers and perhaps Mr. Lavoie, Mr. Boyles and I may give responses to the questions having to do with matters of chartered bank policy in a general way.

That concludes my remarks, Mr. Chairman. I would like Mr. Lavoie, if he would, to make one or two opening remarks in the French language.

MR. LEO LAVOIE makes introductory remarks

in the French language.

THE CHAIRMAN: (French) I will ask Mr. Beauvais to respond to your remarks.

COMMISSIONER BEAUVAIS: (French).

THE CHAIRMAN: Mr. Coyne, I think you might take over throughout.

MR. COYNE: Thank you, Mr. Chairman.

Mr. Currie, I wonder if we could start out by discussing some general thoughts which you have put forward in your brief. May I ask you to turn to page 3, which, of course, is the beginning of the summary of conclusions and recommendations. I have several questions which arise out of this section although, of course, most of the points are dealt with in the more detailed subsequent sections of the brief, and some of the obvious questions I would prefer to have when we come to those sections.

Commencing with paragraph 7 on this page you are commenting on the very heavy reliance thatis placed by the Federal government on income tax, both from persons and from corporations and you say that there can be no question but that the heavy rate of corporation taxation together with a steeply graduated personal income tax must have a very substantial effect on costs of production in Canada, on our competitive position in world markets, and also on the incentives to work and produce, which are the basic driving force of a free enterprise economy.

I would like to take these effects in turn and first of all ask you or your associates to comment on the effects which you feel these taxes have on cost of production. This is not the notion which is regularly brought to us. The theory, in any event, being that corporation income tax take their effect upon income which has been earned after costs have been met.

I wonder if you or one of your colleagues would expand upon the idea you have in mind as to the effect of high income tax in relation to costs of production?

MR. CURRIE: Mr. Coyne, Mr. Keaveney is very well suited to answer that question having had very wide experience in industry as a comptroller. I would like to ask him to answer.

MR. KEAVENEY: Mr. Coyne, I feel that although one would say that income taxes are levied on profits after they have been earned, they are nevertheless still a charge against the overall income of a corporation at any year and merely because they are levied below the line after the profits for the year, before taxes have been arrived at, does not exclude them from a consider- ation as a cost factor.

I feel in Canada the rate of the levies at the corporate level are such as to increase the cost inasmuch as the net margin after tax left to the corporation is, I feel, lower than maybe the case if Canadian manufacturers are going to be placed into a position to compete

particularly overseas.

Would you care to add to that?

MR. CROWE: I don't think there is much can be added to it. I think that was the main point we had in mind. As a practical matter, these taxes are taken into account as a cost in decisions made by industry in deciding upon their operations and I do not think I would need anything to add to that.

MR. COYNE: Are we thinking here to some extent of attempts to shift the incidence of the corporation tax, that is, specifically, on to customers, so that in that sense it might be built into the cost say of a customer from a manufacturer. The manufacturer might endeavour to recover some part of his corporation tax by charging a higher price to the customer, if he could succeed in doing so. Is that any part of the thinking here?

MR. CROWE: Well, I think that may be another factor, yes.

MR. COYNE: In any event I suppose you will agree that your concept of costs in this sense, Mr. Keaveney, are in a somewhat different sense from the ordinary day-to-day fixed costs that big business, particularly manufacturers, have to defray in order to carry on.

MR. KEAVENEY: I think there is a distinction which can be drawn, quite so. I think that the level of taxation can affect a decision, for instance, of a manufacturing company in deciding

whether or not it is going to set up perhaps a new facility, expand its facilities because the guide post used to arrive at such decisions is the net return after taxes on the investment that is required, so I feel that the tax burden is a cost factor in that sense.

MR. COYNE: In the sense that he is considering the impact of taxation in the same way he is considering other costs.

MR. KEAVENEY: Quite so.

MR. COYNE: That would be involved in the operation.

MR. KEAVENEY: Quite so.

MR. COYNE: I wonder if we could turn to the section of general effect that you speak of in this paragraph and that is on our competitive position in world markets. As you may well know, the Canadian Trade Committee recently commissioned a study which was carried out by the Canadian Tax Foundation, I think actually by Mr. Robertson, as to the effects of the Canadian tax structure upon our competitive position in world markets. I have before me an excerpt simply from the introductory statement which the Canadian Trade Committee appended to this study when they issued it in which they sketch out very briefly the conclusions which appear to be justified from this study.

I will just read very briefly from this and ask you to comment, if you would, in the light of your own experience and the experience of

the members of the Association. The introductory statement says:

> " The general statistical comparisons indicate that taxes in Canada, as a share of GNP, are no greater than in most industrial advanced nations. Although Canadian governments appear to rely more upon direct taxes than those of many of our trading partners, this would not appear to place Canadian producers at a disadvantage with respect to the principal sources of Canada's manufactured imports, notably the United States."

And then I am just quoting the general statement that they make here. They say:

> "On the basis of the evidence contained in this report, it would appear difficult to support the proposition that differences in tax systems constitute a major factor adverse the affect in the over-all international competitive position of Canadian industry."

I wonder if you would care to comment on that in relation to the general position you take here?

MR. KEAVENEY: Well, I don't feel that this subject can be considered by merely comparing the average tax burden in Canada and

the average tax burden in other countries. I think one has to take a proper view recognizing that the Canadian secondary industry in particular has got such a limited domestic market that it requires additional incentive if it is going to have the courage to venture into expanded plant facilities in order to generate extra production to sell aborad, and I feel that this extra filip is necessary for incentive in this country particularly.

I do not think it is merely fair to say that the tax rate in such and such a country is higher or the same as Canada. I don't think it is fair to merely limit it to that statement. I think in this country it has become more evident in recent years, and this is well recognized and more and more so at all levels of business and government, that if we are going to cure the problems we have particularly as regards to unemployment and greater utilization of existing facilities and the opportunity of increasing these facilities, it will be necessary for these industries to compete in every way possible, and I feel that the tax burden should be reduced notwithstanding the fact that there may be examples quoted which show that in foreign countries, or in some foreign countries, the overall may be just as high as in Canada. I think this is a very important fact.

MR. COYNE: Thank you. Well then, still in this paragraph you say: "In order to achieve

the maximum incentives for the expansion of business and individual enterprise, strong inducements through tax relief should be introduced".

This, of course, is a general statement but again speaking generally two different views -- well, perhaps a variety of different views -- I would like to refer to two different views which have been urged on the Commission with regard to the type of incentives which are called for. This is strictly an economists argument, therefore I have no views on this subject. Some people state that what is needed is a tax system which will offer incentive to the building up of production facilities, additional investment in plant, and therefore a relief from corporation tax and other tax, the burden of which falls upon business.

Others say that what is needed -- the problem that has arisen in the last five or ten years has been a failure of demand. What is needed therefore from the tax structure is an encouragement to greater consumption, greater development of demand; and it is further cited to us, for example, the experience of 1955-57 when we had a tremendous investment boom at a time when tax rates are as high as they are now. They say this demonstrates that high tax rates do not inhibit investment if demand for products is sufficiently high and vigorous as at the present time. Would you have any comment to make on that general proposition?

MR. CURRIE: May I just add that the intention of the Association Committee was to divide this into two parts. There was this aspect with which you are dealing now. There is another aspect and its effect upon incentive in individual cases.

MR. COYNE: I was really thinking about the very general terms here.

MR. CURRIE: I believe that Mr. Keaveney can perhaps answer the first half of your question. If the second half is the effect on the individual, I can deal with that.

MR. COYNE: I was really thinking in the general terms. I was not thinking of specific fixed incentives along either of these lines.

THE CHAIRMAN: We have had producers, Mr. Currie, tell us that the way relief is needed is to encourage greater investment in plant and equipment. We have had consumers tell us what is required is relief to encourage consumption. There is no sense having equipment if you haven't got a market. The market comes first, the plant comes after. Of course, we are very interested in what you feel the Canadian Bankers' Association might wish.

MR. KEAVENEY: I would like to speak to one particular phase of your remarks, Mr. Coyne. The statement was made that during the period 1955-57 when taxes were as high as they are now, there was a significantly high demand. It was during this

period that there was an extraordinary acceleration in the rate of capital investment in Canada, brought about by some very special circumstances, two or three of which I shall mention. There was first the uranium industry. There was second the major power projects of which the St. Lawrence Power Work and Seaway were the main and thirdly, during that period, for example, amongst the primary producers the paper-making industry installed a very considerable amount of plant and after that plant had been installed, it took care of the capacity required and the demand for a considerable period to come. So that subsequent to that time there was a falling off in capital investment, particularly in those areas, and there was no substitution by way of other special projects.

I just want to register the point that that period in addition was supplemented by still some carry-over of the postwar demand for various products. That was an additional factor. I feel I consider that the period 1955-57 was unusual in the economic cycle we have just gone through.

MR. CROWE: There was another factor in the same economy. We are heavy importers and if you look at this in terms of the two alternatives, no reduction to the producer and give additional income to the consumer, the additional income in the hands of the consumer can, to a substantial proportion reinforce imports so you do not necessarily get the same impact on the Canadian production that

is commensurate with the increase in income. I think that our approach is that basically production must be economic and effective, that if you do not have a sound and profitable base on the production side then it is not really possible in the long run to cure that by simply inflating the consumer's income, and that is part of the economic equation.

We certainly do not dispute that consumption is a vital part of the economic process.

I think the point Mr. Keaveney is making when we take into account the import factor that we feel that it is almost equally as important to ensure that on the production side it is profitable and efficient.

MR. COYNE: Thank you. Well then, I wonder if you go down the page a little ways where you are getting into a general term the question of government expenditures. Again you deal with it later on in your brief in the section that commences on page 11. You say towards the bottom of the page: it is recommended that serious study should be given to the question of whether any portion of the welfare programs, which already accounts for almost one-fifth of the total Federal budgetary expenditures, might be placed on a self-sustaining basis to be financed by premiums paid by those who would normally expect to be beneficiaries.

I wonder if we could examine that in a little more detail in relation to the principle welfare programs that in fact exist and contribute

to these costs of which you speak.

May I put this proposition to you that, for example, the cost of old age security is already on a contributory basis in the sense that used to be 2-2-2 and then 3-3-3 and now it is 3-3-4 rule -- a definite segment of the personal income tax and corporation income tax and sales tax relative to the old age security fund.

I suppose it is fair to say that the new pension benefits, which are being contemplated, are intended to be basically contributory. Unemployment insurance is now conducted on a contributory basis. I suppose the Veterans Pensions and assistance to the Blind and to the Indigent are the sort of things that cannot be put on a contributory basis; which only leaves among the large programs Family Allowances, which, of course, are very large, and which in a very rough manner, some attention is paid to the benefits in that there are differences in the exemptions that are allowed for children who are drawing family allowances.

Then, I suppose, hospital insurance which produces considerable evidence, you may well say, as far as Federal contributions to provincial hospital plans is concerned it is a straight charge on general revenues, but in relation to these existing plans, can you really say there is anything that might be done about them in the light of what I put to you as being the case that many of these plans today bear a strong if not complete

contributory feature.

MR. CROWE: I think, Mr. Coyne, you have pointed out some of the problems that we had in mind. We realize that there is this element already in some of the welfare programs and I think what we really had in mind was that we hope the Commission would be able to examine the whole range of the welfare programs and see whether there was any possibility of any expansion of this principle.

We certainly recognize that there are areas where welfare assistance is definitely needed. There is no suggestion we are going to eliminate welfare assistance in cases where it is needed. We wonder whether by careful examination of all these schemes there might not emerge some possibility of expanding this principle of putting it on the basis of related to contributions in order to try to make the whole thing more effective and to have last in the way of what we feel are undesirable impacts on the economy, but I don't think we are in a position or prepared to try to apply this in detail to specific welfare programs. We really hope that this question may encourage the Commission to pursue this point of view, looking at the welfare schemes.

MR. COYNE: Thank you very much, Mr. Crowe. This is really a general feature that you are putting forward.

MR. CROWE: That is right.

MR. COYNE: In suggesting consideration

of this aspect of the matter. Well then, I turn to page 4 and you discuss in paragraph 9 one of the issues repeatedly raised in Canada, the matter of investment by Canadians in equity stock of Canadian corporations which in turn is related to the high degree of foreign ownership of Canadian industry, and again you deal with this in more detail in the section of the brief commencing at page 13 where you say -- I am looking now at paragraph 32 on page 13 --

> "It would seem clear that the steeply rising rates of taxation of personal incomes must have some impact on this matter. The present taxation system which consists essentially in imposing taxes where they are easiest to collect, impedes creation of capital in Canada. Some changes in the marginal rates of personal taxation could make a significant difference to the amounts of income available for investment.

Then you state the suggestion has been made about the levelling off of income tax rates.

> " Some such modification of the steeply graduated income tax structure would be the most important and immediate steps which could be taken to make possible increase in investment by Canadians in Canadian equity securities."

I wonder if you could comment on an aspect of this problem which came up the other day in a hearing before the Commission. The normal or perhaps naive inference that seems to be drawn from statements about Canadian equities in this context is that there is an enormous amount of Canadian equities floating around and a very serious lack of demand by Canadians for these Canadian equities which would normally result, one would expect, in prices being driven down, and it becomesmore attractive to other than Canadians and this, of course, could lead to heavy purchases by foreigners.

On the other hand, the facts of the situation seem to be, according to someone who appeared the other day, that characteristically at the moment there is a shortage of Canadian equities. Institutions, so we are told, certainly found this to be the case. Some of them, of course, are limited by virtue of eligibility requirements, but pension funds certainly and perhaps to a lesser extent insurance companies tell us there just are not enough Canadian equities to go around. If that is the case, how could you develop Canadian ownership of these equities simply by reducing the taxation impact upon Canadians?

MR. CURRIE: That is a fairly wide ranged plan, Mr. Coyne.

MR. COYNE: Yes.

MR. CURRIE: I think what we are talking about here is the individual rather than the large purchase, or large institutional purchaser. It is very difficult and dangerous to take these things out of context. I think this thought is bound by the thought of incentives which we think comes very high in the progressive context as against individuals. What we are saying is that a high rate of taxation -- progressive taxation, an individual beginning to earn an important annual amount, is thought of as having lost this increase by the high rate of taxation. Now, when you are talking about individual purchasers of Canadian equities, we are not talking about purchasers of some bulk, as you are when you are talking about an insurance company with a pension fund or something like that. I think we could go on to say with some safety that one of the things that distinguishes the Canadian scene is a look at what we might call the middle fortune. There are not a great many large fortunes in Canada, as they are sometimes known to the rest of the world. There are not so many middle ranking forces as you see in the United States.

I would say that this country could be described as a country of wage earners, and those who are affluent are those who earn high wages.

In this regard the thought in the back of our minds was, so long as taxation goes on at the present rate there is very little opportunity to form this nucleai of capital, is certainly less than it would otherwise be. This is the plain object of the case. We are talking here in context with the criticism which might be made that not enough individual Canadians own equity stock.

MR. COYNE: This, of course, Mr. Currie, is a very widely held theory and a very valid one on theoretical grounds. It is very difficult, I suggest, to prove or to demonstrate that lower taxes in the middle range would result in those less heavily taxed persons buying Canadian equities. About all I could suggest to you is that they would have a greater net disposable income to save or spend than they have now.

MR. CURRIE: Whether they buy bonds or equity is, of course, a matter of individual decision.

MR. COYNE: Or whether they buy an extra motorcar.

MR. CURRIE: Yes.

THE CHAIRMAN: It is rather interesting in that connection to look at Appendix 6 which we have had submitted to us, of course, in respect of estates. That shows what people hold when they die. Table 2 on that page shows in the fourth last column stocks and shares. The next column shows bonds and debentures and the next one is real estate.

When estates are small, $50,000 or $75,000, I notice they are pretty secure estates. There is a lot of real estate, and bonds are in about the same amount as equities. Life insurance seems to rank fairly high. But, as estates get bigger, and I suppose it is obvious this would occur, although I found it interesting to look at the confirmation here in the figures, the proportion of equities goes up as against everything else. When one gets to estates of $200,000 or $300,000 the stocks and shares are close to equaling real estate, bonds and debentures, and of course it is a good deal more than one of the other two. Even in respect of small estates the average holdings of stocks and shares is not bad. There are 1,142 estates of $50,000 to $75,000 and the total of stocks and shares held is $13½ million. I think that is about $12,000 each, which I thought was a little surprising because these are rather pretty small estates. So that there are fair holdings of stocks and shares by individuals in all ranges. Of course, as it goes up they become larger.

Am I interpreting the figures correctly?

MR. CURRIE: This was our interpretation.

MR. COYNE: Following along this paragraph, still dealing with the same problem, you say that consideration should be given to providing a greater degree of incentive either by increasing substantially the rate of dividend tax credit or by the adoption of a flat rate of taxes on all dividend

income. You speak of increasing substantially the rate on dividend tax credit as an incentive in this context. It has usually been, or frequently been justified not so much in terms of an incentive but in terms of equity on the basis that, of course, the income is taxed in the hands of the corporation and then is taxed again in the hands of the individual shareholder, and that the dividend tax credit to a substantial extent among the small corporations and to a much less extent in the case of the large corporations, is conceived to offset this, or eliminate some of this double taxation. One difficulty that is put to us in respect of increasing the rate of credit is that it is not a matter of double taxation because there is considered to be a great deal although an undetermined amount of shifting by the corporation to its customers, and perhaps to a lesser extent to its employees. In other words, the impact of the corporation tax is not borne solely by the shareholders. Would you have any comment upon that aspect of the situation or upon the limits to which one might properly be able to raise the rate of dividend tax credit?

MR. KEAVENEY: This ties in, in our feeling, with what Mr. Currie has just said; that is, to encourage the middle group to participate to a greater extent in ownership of equities in Canadian companies. We do feel that if some additional relief be provided through a modification of the personal tax structure which enabled them to

have even some modest amount of extra available each year to put into these equities, that combined with the knowledge that they secure additional tax relief on the income therefrom would, we feel, be an additional incentive toward Canadians getting a greater share of ownership in Canadian companies and would encourage a greater awareness of the benefits of share ownership.

MR. COYNE: Thank you very much. You are really thinking of it in terms of an incentive, as I understand your reply. If you could reduce the impact of these rates that would leave these people with a larger amount of disposable personal income, and if you were able to provide them with an incentive of this nature that might persuade them to put more of this additional income into common stock investment?

MR. CURRIE: Perhaps I could add to these remarks, Mr. Coyne.

MR. COYNE: Yes.

MR. CURRIE: This is a rather difficult thing, and although this rather deserts the terms of reference, it seems to us, and this is my observation, that we are talking about a relatively small class of people here, but they are sensible people, generally speaking, and it would follow that probably they are the leaders of our industry. A country's health, its progress and its strength depends upon this, I suppose, elite , I don't know. They are those who work harder and have more talent. It is our feeling, and very strongly so, where you inhibit

the formation of capital that these people earn by their own efforts, until such time as they themselves become more affluent they are by nature more cautious. This is a reasonable thing. We see it happening all around us. What we need in our industries are people who are able to be aggressive. One of the ways in which this can be encouraged is to make it possible for them to get more of the fruits of their effort. What we are talking about is not an answer in itself, but it is part of the whole background picture, and this is what we mean when we are talking about incentive. If there are financial stringencies in the background of business, almost inevitably they project this into business decisions.

I do not know whether I am explaining this very well to you, but this is not really what we are talking about. We are talking about human beings.

MR. COYNE: Thank you very much.

THE CHAIRMAN: I hope you bear in mind, Mr. Currie, the fact that we do not pay a capital gain tax in this country as opposed to our neighbours. I am sure that to the class of people to which you have referred that must be very attractive.

MR. CURRIE: Yes, that is there and I appreciate it.

THE CHAIRMAN: When you were speaking of the risk, and the nerve to take risks I would have thought if one were going to take a risk, it must be

-7

much more attractive to know that you can receive 100% of the benefit rather than something like 75% of the benefit.

MR. CURRIE: I think capital gains tax is probably less effective because it taxes on the future and those who take the risk, because this is part of the risk if you are in a country which takes a capital gains tax. However, our association is thinking about the beginning of the change.

MR. COYNE: Perhaps we could now turn again to page 5 where you are dealing with a somewhat different subject in respect of estate taxes.

In paragraph 10 you point out that study is also required of the effect of estate taxes and succession duties on ownership of Canadian industry. It would appear that the level of such duties has been such as to force the sale of Canadian owned enterprises to foreign interests and relief in this area should be given through a reduction in the rates of these duties. This again is a statement that is put to us very frequently, but we have had some difficulty in finding any sort of specific evidence that sales of this nature were to foreign enterprises or to others and actually dictated by death duties as such rather than other factors which normally take place in a small privately owned business upon the death of the principal owner-manager. Does the bankers association have anything that might be considered as evidence as to this sort of thing indeed taking place which would represent very widely

the idea of the sort of persons who have knowledge of the circumstances?

MR. CURRIE: We had some serious second thoughts about this, Mr. Coyne. I am quite certain that most of the people who advance this thought had something specific in their minds when they did so. Bankers from time to time see examples of this, but I think that we have possibly not expressed this as well as we might have.

What we are really saying here is that inevitably this makes the climate seem salubrious. With this type of situation I think you can go further and say that in the context in which you have a much more affluent society to the south of us, for example, looking for purchases with the cash available, this is the type of result. I think we agree with you that it is very hard to document this and show by specifics how this happens. This really was a series of individual decisions.

MR. COYNE: It is very interesting to hear you mention, of course, our proximity to the affluent neighbour to the south. For example, they have a very heavy death duty in the United Kingdom; far heavier than we have, and no doubt frequently small businesses are sold upon the death of the owner, but I doubt whether it is of any concern to them in the United Kingdom that some of these private businesses are sold to persons abroad.

I do not know that, of course.

Then going on to the very interesting suggestion which you make in paragraph 11, and this concerns exemptions under the estate tax act which you deal with at page 29 and following, you make several suggestions in respect of exemptions, and at the bottom of page 29 you recommend that there be a basic exemption of $50,000 in all estates. I understand that to mean an increase from the $40,000, and that the additional exemption of $20,000 for the estate of a deceased male person survived by a spouse be increased to $50,000, the other personal exemptions remaining as they are. Then you make the suggestion over in paragraph 80 at page 32, which is repeated in the paragraphs of which we have been speaking. A valuable incentive to Canadian ownership of our industry could be provided at a very nominal cost through providing exemptions from estate tax for domiciled decedents for portions of estates which consist of stocks of Canadian corporations up to a value of, say $50,000. You suggest that the figure of $50,000 is only a suggestion, but it is the principle that you are principally recommending.

Looking at the details of how an exemption of this kind might work in practice, I am wondering whether you have in mind that this exemption for common stocks would be an additional exemption over and above the existing personal exemptions, or how would it work in practice in your

mind?

MR. KEAVENEY: It would be a supplementary exemption.

MR. COYNE: It would be really an additional exemption. If there were an estate in which the decedent was a married man, leaving a widow which had $50,000 in common Canadian stocks, would it follow that that estate would then have first of all the basic exemption of $50,000, the widow's exemption of $50,000 and, as is your recommendation, an additional exemption for common stock, being a total exemption of $150,000?

MR. KEAVENEY: Yes.

MR. COYNE: Whereas if the same estate was completed real estate or bonds it would be $100,000?

MR. KEAVENEY: Yes.

MR. COYNE: Thank you.

THE CHAIRMAN: One would then omit, I suppose, totalling up the estate in respect of the common stocks up to the amount of $50,000 in arriving at the total evaluation?

MR. KEAVENEY: Yes.

THE CHAIRMAN: So it would be the first exemption, really? It would not really go into the amount?

MR. KEAVENEY: It would be excluded.

COMMISSIONER WALLS: Would that not leave small businesses and farmers incorporating, issuing shares to themselves and almost completely

escaping estate taxes?

MR. KEAVENEY: This raises an interesting point, of course. The main purpose of our suggestion is that it be explored. Certainly this, Mr. Walls, would have to be studied. I quite agree with you in that regard.

THE CHAIRMAN: You are not laying down how much should be done, but Mr. Walls has brought forth a point. Even if you restrict it to listed companies they probably would find a way to have a large firm get some kind of a listing, and administrative difficulties might be such as to rule it out.

MR. COYNE: Then the next point that you deal with in the summary at page 5 is the question of credit unions and the tax status which they enjoy. You also, of course, develop this thought at greater length at pages 15 to 17. I have just one question that I want to ask you here and it arises out of the second sentence in paragraph 12 at page 5 where you say:

> "It is recommended that the present tax advantages conferred on credit unions should be closely reviewed, especially as they relate to those which have attained a large size and whose activities have become increasingly indistinguishable from other financial enterprises."

My question is, are you suggesting here that something different should be done in respect of the tax status of credit unions based upon size, which seems inferred here, and is an interesting thought?

MR. CURRIE: Perhaps Mr. Crowe will respond to that observation.

MR. CROWE: We certainly do not want to single out size as the sole criterion. We have said: " -- especially as they relate to those which have attained a large size and whose activities have become increasingly indistinguishable from other financial enterprises." I do not think we put the weight on the word "especially". We are not excluding others. We are putting the emphasis particularly on the kind of activities they are engaged in, to the extent they are engaged in activities that seem to include commercial loans and that sort of thing which are indistinguishable from other financial enterprises. We feel it probably becomes more serious in this regard but we are not really trying to set out any detailed proposal, nor suggesting any specific area where this could be applied, or the tax could be applied which might exclude some and include others. Size seemed to us to be a factor but we certainly do not regard it by itself as the only criterion.

THE CHAIRMAN: Are you coming back to this summary,then moving to the main part of the brief?

MR. COYNE: Yes, I was going to take

that now, Mr. Chairman. I was going to move down to the summary and thenmove into the specific matters which are dealt with in part 3. Which one did you want to come back to, Mr. Chairman?

THE CHAIRMAN: The one you are on now I think we ought to explore fairly carefully before we go through it. I raised the question to establish whether or not this was the time to do this.

MR. COYNE: For my own part, Mr. Chairman, this would be quite a convenient time to deal with this.

Arising cut of your answer, Mr. Crowe, is it fair to say that what you are speaking of here following the word "especially" is your thought that merely this is the reason why perhaps credit unions are now subject to a different tax status than heretofore? You are not suggesting there are any reasons for classifying credit unions, some which should be tax exempt and some which should be taxable?

MR. CROWE: I think that is right, yes. We feel that because of the size question things should be reconsidered in respect of size and other factors including the kind of activities, but we do not suggest, as you point out, that size itself should be a determination in respect of the kind of tax treatment.

MR. COYNE: That was the only question I intended to ask in respect of credit unions, but

since this has been raised, if the Commissioners have any questions on pages 15 to 17 where this subject is dealt with it might be a convenient time now to ask those questions.

THE CHAIRMAN: I am not sure you have not already got the answer I was looking for. All I wished really to inquire into was whether these gentlemen believe there are any credit unions in existence which merit a tax exemption status. The McDougall Commission I think recommended they be not taxed because they were rendering a very favourable service, and it felt that the service might be impaired through a tax position. However, we are beyond that position now. That was a long time ago. They have developed immensely since then. I was wondering if there is a case for any of them to escape taxes.

MR. CURRIE: Perhaps to answer that in another way, Mr. Chairman, I should state that I think what we are talking about here is credit unions or co-operatives which have far outstripped the original concept of the community interest with benefit to a distinguishable group. It seems to us that where circumstances are such that the organization now competes in the broad market but at the same time supported by a tax advantage, this is something the Commission may wish to look at.

THE CHAIRMAN: Of course that is obvious. The Commission is already looking at this. We have

already received representations on this score and we are certainly looking at it.

MR. CURRIE: As bankers we run into this particularly in the credit union field because in communities, of which we are well aware, the competitive force of the credit union is a public service and grows and grows, and has moved far out of its original field for the mutual benefit of its members, and now competes for commercial loans and for municipal loans. They are now looking to more and more fields in which they can invest their funds yet they still retain the tax advantages which were there in what you might refer to as a rather more modest beginning. Which type of credit union would be the most objectionable competitively? There are all kinds of industrial ones, I presume, collecting their deposits by payroll deductions, which seems to be the convenient and sensible way?

MR.CURRIE: Certainly I was not speaking about this. I am thinking in my mind more of a credit union which has now set up a premises for itself and does general business with the general public. Saskatchewan is one of the places where you see this, and British Columbia is another province where this has taken place. You speak of an industrial commercial union. This is really and usually made up of people engaged in the same locality, the same plant and in the same premises.

THE CHAIRMAN: Was that the reason for

16

the tax exemption for an industrial credit union?

MR. CURRIE: That is a question I do not really think I can answer, Mr. Chairman. I am not familiar with the history and the beginning of the reasons, although I can appreciate the situation.

THE CHAIRMAN: I am trying to find out how generally your suggestion as to taxation of credit unions would apply, and particularly whether this suggestion applies to all of them, or the ones you say you are thinking of, those which are like small banks.

MR. CURRIE: That is right. I think we have not gone this far. I think any development along this route would need a great deal of discernment as to which credit unions are taxable; at what point do they become taxable and under what conditions. It was not our intention to lay out a plan or proposal as to when this should be done.

COMMISSIONER WALLS: We have had the reverse inference placed before this Commission as to which came first, the chicken or the egg in respect of two items; first of all, credit unions that have organized themselves industrially, and went into that business when the banks showed no sign of going into that business, and that criticism laid to the banks going into the small personal loan business, which they had not entered before. I would be interested in knowing what your reaction is to these two statements.

MR. CURRIE: If I may commence at the

moment by saying that my employer certainly does not fall within that category because it introduced a personal loan plan in the 1930's. It was alone in this regard for a great many years until the other banks examined some doubts they had about this type of a scheme, and eventually we saw that the consumer type of loan became available through all banks. All of the plant type credit unions are customers of the banks. I do not say this is something which the banks complain about. There are areas in which it is profitable and in which there is a need for the bank to enter. If 20 people in a plant bind together and can service the requirements of small loans, which is in my mind at any rate a matter of individual decision, this is not necessarily something in respect of which the banks should enter, because it is a very small field. Banks are rather more concerned with their services in the over-all field.

Am I going the way of your argument, or have I deserted it?

COMMISSIONER WALLS: Have you finished with your answer?

MR. CRAIG: Yes, if I have understood the question.

COMMISSIONER WALLS: Well, on page 16 you say compared with chartered banks and Provincial Government savings offices credit unions have grown at a much faster rate in the past 14 years and one of the principal reasons underlying credit union growth has been the higher rate of interest that they are able to pay depositors. Contributing substantially to this has been their exemption from income taxation.

Now, is it not a fact that growth of savings services by trust companies has grown just as fast, if not faster than credit unions and certainly that cannot be in any way credited to taxation because if anything, their tax is even more strict than the bank.

MR. CURRIE: The reason for that, of course, is they can invest their funds in heavy yield equities paying six per cent. I am speaking of the trust companies. I suppose it might well have been added that in section 42 that credit unions have grown at a much faster rate in the last 14 years and one of the reasons is that they are able to pay a higher return on their deposit because they are not so heavily taxed. Another reason would be that they also charge more for their -- they are getting a bigger yield on high earning assets such as loans. Another reason is that the expenses of a small -- the expenses

of a small virtually voluntary group as to the establishment are very small. A great many of their people work without pay which, for example, is well known so that there are a great many reasons for this tax advantage they enjoy; but they can pay higher rate to their depositors --

MR. BOYLES: They are not subjected to the same reserve requirements.

MR. CURRIE: This, of course, really spills over into the Bank Act.

COMMISSIONER WALLS: Would the banks accept all of the type of loans that are today transacted by credit unions or their members? In other words, are they not contributing a service that you are not compared to compete with.

MR. CURRIE: This is very dangerous ground on which to generalize, Mr. Walls, but to the extent that credit can be given, those who enter the doors of banks today for this type of loan very rarely go out without their needs being satisfied.

There is an added propinquity here because it is a great deal easier for a man in a plant to arrange for a loan in his lunch hour or something like that rather than walk four or five blocks to the bank. Our Association is not addressing its remarks to that type of organization.

THE CHAIRMAN: I find it hard to distinguish between the ones that you do and the ones that you don't; The ones that you don't address yourself to are in-plant credit unions, I take it? Are there others in that category of which you are thinking?

MR. CRAIG: Well, another type would be in those towns in which no branch bank has established itself. There are a great many towns which are served by credit unions. It is the only financial service in the town. These are cases, whatever the reasons might be, that no branch bank has ever seen fit to enter that particular area to establish a branch. This is another type.

THE CHAIRMAN: You are simply saying this: You are not concerned about whether these are taxed or not taxed. You are not suggesting they should not be taxed.

MR. CURRIE: No, we have not said that. We have not dealt with that. We were only dealing with those we think ought to be taxed. Those are the ones that compete directly in the services which we offer and which obviously compete at an advantage but compete on the same scale. We need not attempt to split up which one becomes taxable and which are still allowed this advantage.

THE CHAIRMAN: That is our problem. It is a very real problem as to whether it is a business or whether it is a business that exists for financial gain or whether its just a business. I don't know. These things will have to be decided upon. That is our work.

MR. COYNE: Well then, I wonder if we can turn from other parts of this section, which we will pick up in the body of the brief to section B which deals with government revenues and expenditures

and taxation policies.

I would like to turn to page 14. Mr. Chairman, perhaps some of the Commissioners might want to go back when we finish with this section.

I am looking at paragraph 36 where we are dealing with questions that we have discussed earlier, namely investment by Canadians in Canadian equities. In paragraph 36 you deal with another point. You say:

> "Another related factor is that the present tax system tends, in general, to discourage equity financing in favour of either debt financing (where the interest cost is a deductible expense) or the use of internal funds."

Picking up this part in parenthesis there, where the interest cost is a deductible expense, do you think that the fact that interest is deductible and of course dividends are not is really an important factor in causing businesses to prefer debt financing or internal financing to finance their equities?

MR. KEAVENEY: I think it is difficult to answer that question in a general way. The decision of the corporation in issuing new capital is predicated on various factors. Certainly one would be the tax aspect and deductibility of interest in the event of a bond issue but in addition corporations in issuing capital do have to keep an appropriate balance. Generally speaking there is an attempt to

keep an appropriate balance between funded debt and shareholders' equity.

MR. COYNE: This is the balance not affected by tax factors.

MR. KEAVENEY: No. There are general principles. There are no set principles. There are general principles followed in keeping a reasonable balance which does vary, of course, from industry to industry but as we have said here and I repeat that the fact that interest balance is deductible no doubt is an important factor in reaching such a decision.

As bankers, we certainly feel it is proper that there should be appropriate encouragement to finance internally. Further the corporation is in a position to build up a strong working capital position and maintain its general financial position on an improving basis. As we say, we certainly do not suggest for one moment that anything should be done to discourage that aspect.

MR. COYNE: Whatever may be the effect of the problems of interest as compared with the problems of dividends, you are not making a specific recommendation to put them on an even basis. Sometimes it is suggested that dividends be deductible in effect from corporation income tax by moving them from distributed earnings. You are not making any suggestion of that kind. As In interpret this part of your general recommendation, it is that some reduction of the impact of income tax would likely contribute to some development to equity financing.

MR. KEAVENEY: Yes.

THE CHAIRMAN: Mr. Coyne, I wonder whether you would agree with the investment dealers upon this point that there is an advantage in a fixed interest on financing. They also point out that of course while a company may prefer this by way of financing, the investors themselves think of a dividend credit and the interest in securing a dividend credit in respect of dividends which are not available to him by way of interest. They implied there was a force moving in opposite directions and in fact I rather gathered the impression they felt the influence of the one was not far different from the influence of the other. Do you think that would be true?

MR. CROWE: I don't really think I have any --

MR. SAUNDERS: I couldn't follow your reasoning on that.

THE CHAIRMAN: A company when they issue bonds gets an advantage from the deduction of interest. A shareholder, when they issue stocks, gets the advantage of the dividend credits. Therefore, one prefers interest and the other prefers dividends. I suggest to you that that may cause a neutrality with regard to taxation if one would feel the benefit of the other. Therefore, taxation is not an influence in choosing interest as against dividends. Is that clearly stated?

MR. SAUNDERS: I don't know how we could

comment on that. There would have to be quite a study required.

THE CHAIRMAN: Your suggestion is that the deduction of interest provides an imbalance in favour of the issue of bonds and causes more financing for bonds than would otherwise be the case if there was no tax. I suggest to you because of the dividend tax credit the influence about cancels one another and the distinction as between bonds and stocks remains pretty much the same as if there was no tax. Would you agree or would you not agree with that statement?

MR. KEAVENEY: I think on balance I would be inclined to feel that the fact that interest is deductible would be an important factor.

THE CHAIRMAN: The dividend credit would not be an important factor?

MR. KEAVENEY: I feel it would outweigh or equal the other.

MR. CURRIE: Quite frankly, I don't think that this is a question which has been discussed by this Committee, Mr. Carter and I think most of the things I have read about these matters or the arguments I have heard, on reflection, I think this is something we should not go into simply because we have not prepared ourselves along that particular line.

THE CHAIRMAN: In any event the effects of these two taxes would be reflected in the market price as to what of the two kinds of services would be issued.

MR. CURRIE: Yes, and the dividend would be higher. The appreciation would therefore be higher on stocks.

THE CHAIRMAN: One other thing you said in this connection was that there should be nothing done to in any way discourage the accumulation of earnings, the plowing back of the earnings and financing from that source. We have had people say that when that is done that it escapes the market test. Lots of people have said to us that reserves are better distributed and better used if earnings are paid out in dividends and then the company goes to the market to secure its money. I gather that you do not really share that view, a view which usually starts the idea that there may be some kind of higher tax on undistributed earnings. Some European countries, you probably know, tax undistributed earnings a good deal higher so as to force them out and, they say, improve the market. Whether it does or not, I think is questionable. But you do not believe any treatment like that is required in Canada?

MR.CURRIE: I would think this is not a question that bankers would answer objectively because they are concerned very frequently you see that companies accumulate working capital and it is very hard for us to desert the narrow view in this. I think the reasons are perfectly plain.

MR. KEAVENEY: Yes, I think so.

THE CHAIRMAN: I think that brings us then to section C, Income Tax, commencing on page 18.

I don't know whether you would consider this may be a good time for a break.

THE CHAIRMAN: Yes, I think it is a good time to break. We will stand over for 10 minutes.

---Short Recess.

---Upon Resuming.

MR. COYNE: Well, first I would like to turn to page 19 where you discuss this very interesting suggestion about consultation. I think it is quite clear. You say in paragraph 50:

"He should, instead, be able to refer to the competent tax authorities of Canada and the foreign country, jointly, matters relating to his foreign operations, including, where this is feasible, plans which he has in mind with regard to his foreign business, and get from them a ruling on the tax aspects."

In other words, you are really suggesting there should be facilities for obtaining advance rulings in the international field which has frequently be referred to us in the domestic field an advance ruling of a kind should be available. Do you foresee that there might be any administrative or practical difficulties in this field?

MR. CLENNETT: Well, I don't think so. Really, the sort of problem we encounter is that most of the banks engaged in international banking, we have

transactions in many countries and many currencies both for Canadian and nationals and for residents of other countries. The problem from our point of view is largely one of allocation of income. We want to know before we go into a transaction, if possible, certainly before we file our returns because there are problems arising there which I will mention later, which country is going to tax a given transaction.

In nearly all the countries where we have major problems of this nature, the more important ones, we have tax treaties with those countries; if the treaties contain a reference for consultation and so on and this tax applies after you have had an assessment, after you have had a different interpretation and so on. Some people come to you and say "can you do this" and "what will the rate be" or some such thing. We want to be in a position -- in fact we have to to say what we can do. Somebody cannot wait until you get rulings at the present rate. That is the sort of thing we are looking at now.

MR. MALTBY: I think this is probably true as a matter of fact for any Canadian taxpayer. He has foreign operations. He would like to know as early in the day and preferably in advance, as possible what the decisions of the two tax bodies are or are likely to be.

MR. COYNE: I suppose there are, as you have pointed out, two aspects to the problem. One is to know before you embark on a particular transaction how it is treated and even after you have embarked on

it it is useful for you to know how it is going to be treated before you file your tax returns for the period by reason of the foreign tax credit implications to which you refer later on in the brief.

THE CHAIRMAN: I would think that an appointment of somebody in the Department of Finance to take care of that would not be its proper cure. It seems to me he would not be in a position to say much more than you can do yourself; that is to know the law and interpret the law.

One would have to make sure that in a country where we think perhaps there should be someone to whom he could turn for an interpretation, which is a pretty wide recommendation. It might be quite a reasonable one, but I am quite sure as to the frequency of such queries or the need for such information. Is it a sort of day to day matter that a man sitting in the Department of Finance would be kept reasonably busy providing information for these things and spending his time communicating with other countries and so on or is it something that arises once every three weeks?

MR. CLENNETT: I would think in this, Mr. Carter, it would not be a permanent full-time occupation for somebody in the Canadian Government or the Civil Service and a counter-part in other major countries in the world, but we feel that -- you are perfectly right when you suggested that what we had in mind was a facility or similar service in the other country involved. We feel that the present

processes, while certainly operating in the spirit we are looking for, but the timing is not good enough and within the present system of framework that something could and would be desirable to expedite the process, which would mean a part-time job for somebody here. It would not be a frequent reference.

THE CHAIRMAN: It is very easy to understand the difficulties which arise and the need for this. It is hard to comprehend really the seriousness of the impact. I know it causes trouble and difficulty but does it actually prevent transactions? Are there transactions which are not undertaken at all because of such difficulties?

MR. CLENNETT: Well, it has a double impact. In the first place with regard to whether one would say you do something or whether you don't do it, I would think that would not be true. It is hard to generalize because we are aware of the broad provisions of the treaty. I find it pretty hard to visualize a situation where we would say we would not do something because we may have to pay tax where you have trouble with a treaty.

Our greater problem lies in the area where we will go ahead and enter into a transaction and have the problem of determining to which country we should pay the tax. It is not a question of whether the transaction should be taxed or even a question of how much profit is involved, but who is going to get it and if we do not get it the way the countries ultimately agree it becomes a matter in dispute and then we are penalized by virtue of

interest payments as we have explained in the brief.

THE CHAIRMAN: Supposing now you have a difficulty of this kind and you put it to the Finance Department and they say,"of course, it depends on the other country" so you suggest to them that they go and communicate with the other country and try to resolve it between themselves before you proceed or before you file your returns. What happens then? Do they say it is impossible?

MR. CLENNETT: I am given to understand that -- perhaps Mr. Maltby would know more about this -- I understand that in fact it is the understood procedure by and large they only deal with the problem when it arises.

THE CHAIRMAN: Could you not push them into dealing with it before because that is what you are really asking for here.

MR. MALTBY: Perhaps I may say in my experience when we have put something of that nature before the Finance and Revenue they have told us we should come back when it was -- they are very pleasant-- I mean we should come back when the other country has passed judgment on it and not before and we are anxious that there should be joint consideration and in fact other countries should not have been forced into a decision from which they might be later moved by Canada and if there were more review and joint consultation that they would not have to be dislodged from the position they had taken earlier.

20.

At the present time we have not succeeded in having National Revenue take it up on our behalf -- until there is an assessment, I suppose.

MR. COYNE: Mr. Chairman, just arising out of that discussion, would it be fair to say that to some extent or in some sense this suggestion is alternative to the other suggestions that you are making, to which we will come in a moment, in the sense that if the other suggestions were adopted most of the difficulties which now flow from this lack of liaison between the countries would at least be ameliorated.

MR. MALTBY: They would be ameliorated. Decisions would be helped by knowing early, preferably in advance, as to what the course of the two governments would be.

MR. COYNE: Then the following pages set forth the sort of difficulties which you in fact face in this field, particularly with respect to interest penalties as a result of the general provisions relating to the assessment of interest on underpayments and, in paragraph 58, on page 23, you speak of possible cures for this difficulty and you say:

"If this interest on underpayments and overpayments of tax in Canada were, like the United States, calculated at 6 per cent and accountable in the tax return as both income and expense, this anomaly would not arise. If it is felt that there are good reasons which make such general provisions

undesirable, then the penalty should at least be eliminated when it arises from mutually agreed reallocation of taxable income among jurisdictions."

I think you are pointing out there that there could be a simple general amendment to put us in the same position as the United States, which is what you are suggesting in the first sentence that I read, but that even if, for whatever reasons, it was not felt that a general amendment was called for there could in your view be a specific amendment that could deal with this particular situation affecting reallocations of income between countries.

Is that what, in effect, you are suggesting?

MR. MALTBY: Yes, Mr. Coyne, we feel there should be.

MR. CLENNETT: I think on that it is only on the 6 per cent that a complete penalty or cost is avoided; that any other treatment, unless you are going to pay a definite rate of interest, would leave you still subject to variation in rates.

There are two factors involved. There is one factor that we have a different rate for underpayments, for example, from overpayments, which is not the case in some other countries such as the United States. That is one factor in itself, and that particular feature can only be corrected by an equalization of the rates and equalization up to the level of a foreign country.

Then there is the separate factor that if that were not corrected then at least the penalty, if you want to call it that, or advantage which the tax department gets from the interplay with these sections of the Act could be eliminated by a simple amendment.

MR. COYNE: In other words, to completely eliminate any effect at all would require amendments along both the lines of which you speak?

MR. CLENNETT: That is right.

MR. COYNE: And these could, I suppose, be induced -- certainly if you were changing the interest rate to equalize it on underpayments and overpayments -- by general amendments applicable to all taxpayers or presumably by way of some special arrangement related to the carrying on of business in foreign countries and the effect of the foreign tax credits under Section 41.

MR. CLENNETT: That is right.

MR. COYNE: Is that correct?

MR. CLENNETT: That is correct, yes.

THE CHAIRMAN: I would have thought that your proposal might be considered by Canadian banks to be rather unfair. If I were to get 6 per cent interest by overpayment of taxes it would certainly be much in my interest to take all my money out of the bank to overpay taxes. Likewise, if I am going to be allowed a tax deduction for short payments, it is a nice way of borrowing money without having to meet the test of solvency -- and pretty bad banking I would have thought.

While it seems rather unfair that the interest charge should not be permitted as a deduction and the three per cent should be included in income, that could to some extent I suppose be straightened out by leaving the three per cent out of taxable income, but it does not meet the point that you raise, though it goes part of the distance. I really cannot see a very good precedent for the interest rate being the same both ways. Certainly it is not the practice of the banking fraternity. When one borrows money one expects to pay more than when one deposits money.

MR. CLENNETT: It was because of that feature that first of all we set out an easy way of solving the problem, or that particular problem, but it is because of the practicable difficulties that you have pointed out of equalizing the rates, that I pointed out a minute ago, that if we find another cure within the regulations, particularly for people in this situation, it would still not correct the disparity in the rates when you are paying in two jurisdictions.

The reason I mention that is because it bears back on the previous discussion we had with regard to rules prior to assessment. But as you can see, it is important that we get an advance ruling prior to assessment because if you end up with a rate variation, even if you can remove the present problems because of deductibility or otherwise, you still have the rate variation between the two countries as you are paying one rate to one country and one to another.

We appreciate it would be difficult for Canada to pay an extra three per cent because they are paying to the United States. What we hope is that we can solve this by having the allocation agreed upon in the first case.

MR. COYNE: In other words, if there was no reallocation after the event, this particular problem would not arise?

MR. CLENNETT: That is right. Your re-allocation can come from two things: One, it can come from a particular problem or particular transaction on which there is a question on which you would wish to get a ruling before you filed a return; and beyond that circumstances can change and perhaps imperceptibly, and you can have an agreed upon formula for allocating costs which, over a period of years deviates slightly from reality and no one is too concerned and then suddenly one government says, "Look here, this is all wrong", and then they review the procedure completely. In that way you can get a reassessment which is retro-active and you can become involved in interest penalties.

MR. CURRIE: I feel bound to say that I cannot conceive of a situation in the context of which we are speaking in which there would be any advantages deliberately taken of this sort of thing.

MR. CHAIRMAN: So far as international transactions?

MR. CURRIE: Yes. I think the injustices would be evident and the corrections would be matters of judgment, or should be.

MR. COYNE: Is it true that in the United States they pay interest at the rate of six per cent on overpayments and charge at six per cent on under-payments?

MR. CLENNETT: That is correct. I believe as the amounts become excessive then it is very seriously examined, it is no longer a matter of form. But for nominal amounts you get a refund with interest more or less automatically. If it is a large sum of money, they look at it quite seriously; they look at it carefully to see you are not getting the six per cent for nothing.

MR. COYNE: And all taxpayers are allowed to treat interest paid as an expense or as a deduction?

MR. CLENNETT: I believe so.

MR. SAUNDERS: Yes, that is right.

MR. MALTBY: Yes.

MR. COYNE: Then the next subject you comment upon is the treatment of charitable contributions, again in this international context, and in paragraph 64, you point out that:

"By contributing $200,000"

-- you are speaking of the example immediately preceding this paragraph --

"to Canadian charities the corporation reduces its tax bill by $50,000, equivalent to only 25 per cent of the donation -- not the 50 per cent to be expected or by which the tax bill would have been reduced if the

outlay had been, say, for advertising rather than welfare contributions. This is an anomaly which should not be allowed to persist and it is recommended that for income tax purposes charitable donations by a corporation should be treated as an expense in the computation of income rather than as a deduction in the computation of taxable income."

Does this type of anomaly only arise in the case of foreign tax credits and the application of Section 41?

MR. CLENNETT: That is right.

MR. COYNE: It does not arise, for example, in the field of provincial tax credits?

MR. SAUNDERS: I do not think so, no.

MR. COYNE: Then if it only arises in this field, would a more limited type of amendment than the one that you are suggesting here -- which in language is of a general application -- meet the difficulties you have in mind?

MR. CLENNETT: I think it would really. We have made certain suggestions, but they are only intended as suggestions. Anything that would resolve the problem and which would not reduce the tax credit because you made a donation to a Canadian charity would be equally desirable.

MR. COYNE: I suppose you might almost be led -- and I am speaking generally of several of these

recommendations -- into the position of producing a separate code for the computation of the income of the corporation where the corporation also had foreign income?

MR. SAUNDERS: On that, I think it is branch income that is causing the problem.

MR. COYNE: Yes, that is what I mean; I mean branch income not dividend income, of course.

One further suggestion is that this type of amendment would be necessary for a corporation. My question is as to whether individuals would not be affected in the same way -- I presume individuals in business or individuals merely enjoying earned incomes.

MR. CLENNETT: I think so. That must be loose phraseology.

MR. COYNE: You would agree that an amendment of this kind would have to be made applicable to appropriate circumstances, not necessarily limited to businesses carried on in a corporate form?

MR. MALTBY: I would not say from Section 41(1)(a) that this is applicable to a corporation in particular.

I might add that the brief is setting forth donations by a corporation and not by an individual because the corporation's role in making donations is to further its business, and that they should be deductible in the computation of income, that they should be an expense perhaps under Section 11.

MR. COYNE: Then really, Mr. Maltby, you make this point in the succeeding paragraph, paragraph

65.

MR. MALTBY: Yes.

MR. COYNE: And you point out that the Canada-United States Reciprocal Tax Convention deals with this matter as far as United States branch income is concerned but there are not similar provisions with regard to such expenditures in other countries.

MR. MALTBY: Yes.

MR. COYNE: Then you go on, and you are speaking now of donations to charities abroad where the company is carrying on business and you say:

> "Such expenses should not be disallowed per se as charitable donations but should be granted as deductions except to the extent that they offend Section 12(2) as not being an expense 'reasonable in the circumstances'."

There may be some looseness of language, if I may say so, in respect to the use of the word "deductions". You say:

> "... but should be granted as deductions except to the extent that they offend Section 12(2) as not being an expense reasonable in the circumstances'".

That, of course, deals with expenses.

Perhaps you could elaborate your thought there. I take it that you suggest that they should be allowed as deductions?

10

MR. MALTBY: Expense deductions.

MR. COYNE: I am sorry, deductible expenses.

MR. MALTBY: Not allowances.

MR. COYNE: Within the meaning of Section 12(2).

MR. MALTBY: To the extent they are not excluded by Section 12(2).

MR. COYNE: Does your suggestion mean really that with regard to this type of expense or donation the general limitation in Section 12(2) rather than the percentage limitation in Section 27 should be applied, or would they both have application in this context?

MR. MALTBY: Under this proposal the corporation donations would no longer be an allowance granted in the computation of taxable income but an expense deductible from taxable income. That would apply to all charitable donations.

MR. COYNE: Does it imply that any percentage limitation would disappear generally as far as corporations were concerned?

MR. MALTBY: Except to the extent that they became unreasonable.

MR. CLENNETT: Mr. Coyne, I think the point is that these are not permitted at all now abroad. For example, if you were to give, say, $1,500 to the Red Cross in Venezuela under the present Act that is not permitted in the expense deduction at all. That is the purpose of this thought -- to have somewhere in the regulations a provision that such donations be

permitted as deductible expenses.

MR. COYNE: I follow that, Mr. Clennett, but there are perhaps several ways in which this could be dealt with. For example, you might be entitled to make charitable donations in Venezuela up to ten per cent of the income you derive from Venezuela, or you might be permitted to deduct ten per cent of your over-all world income for charitable purposes without distinction of where the charitable donations were made, whether abroad or not.

MR. CLENNETT: I do not think we have pursued our thinking to the extent of the limitations or the exact means by which it would be accomplished. Virtually anything along the lines which now prevail for Canadian donations would be equally satisfactory a solution as long as we do not get into the tax credit problem.

THE CHAIRMAN: Something equivalent to the present allowance put into Section 11 would satisfy you perfectly well, I would take it?

MR. CLENNETT: Yes.

THE CHAIRMAN: That is with a percentage limit?

MR. COYNE: I take it you are really making the general point that you are bound as a matter of good business practice to make these donations in various countries, but at the moment they are not recognized in any respect for tax purposes other than in the United States.

MR. CLENNETT: That is right.

COMMISSIONER WALLS: In view of the records of Canadian corporations and people in high income brackets only using this ten per cent deduction to a very limited extent, based on the taxation records, how big an issue really is this in regard to donations for foreign countries?

MR. CLENNETT: That is a difficult question to answer, but your real problem is that we are in business in these foreign countries to make money for ourselves, and for our shareholders, and in doing so we compete with other institutions which either are local and are permitted these deductions under the local laws or maybe other foreign interests domiciled in a country which still permits these under the existing laws of their country of origin or domicile. The Canadian banks are at a disadvantage in this respect and any other taxpayer is also; it is not restricted to banks. Any Canadian competing abroad in such circumstances is at a disadvantage compared to his competition.

It seems to us that it is undesirable in that our own country should place us at a disadvantage in our efforts abroad when we should be helping the Canadian economy.

COMMISSIONER WALLS: There are companies which would be quite willing to expend the ten per cent abroad which will not expend the ten per cent to Canadian welfare.

MR. BOYLES: Mr. Walls, in respect to your earlier question as to the extent of these contributions

which can be made, they can be quite sizeable. You can get into special circumstances such as disasters. We saw this in Florida when the banks were asked and did indeed contribute sizeable amounts to respective relief funds. You get situations, as it were.

COMMISSIONER GRANT: Mr. Coyne, does not the Canada-United States Convention recognize the charitable donations as between those two countries and recognize each country's contribution?

MR. COYNE: As I understand it, yes, to the extent that donations are made out of income arising in the United States.

COMMISSIONER GRANT: What we are discussing is those countries which have no reciprocal arrangements?

MR. COYNE: Yes.

Then the next subject with which you deal on page 25 is the question of a carry-over of foreign tax credits. In paragraph 66 you say:

> "Because methods of computing taxable income differs from one tax jurisdiction to another, a Canadian business with foreign operations may frequently find that its profits from those operations are taxable in Canada and the foreign country in different years. In those circumstances the present provisions of Section 41 of the Income Tax Act will not prevent

double taxation even though that is the intent of the section."

What I would like to ask you is whether, admitting that Section 41 does not prevent the double taxation for reasons you indicate, there is any possibility of finding relief in the general provisions against double taxation in these conventions, for example, Article 16 of the Canada-United States Convention which you have quoted on an earlier page.

I think the intent of the Convention is to avoid double taxation. If double taxation were to arise because of the deficiencies in the foreign tax section of the statute, would it be possible in your view to claim any relief under the general provisions in the conventions?

MR. MALTBY: It might be possible but I understand that there have been cases where it has failed.

MR. COYNE: It has been tried, in other words, Mr. Maltby?

MR. MALTBY: So I understand.

MR. COYNE: But has it failed because the Canadian authorities felt the Convention was not applicable or because they, having initiated discussions with the other country, were not able to resolve the difficulty?

MR. MALTBY: I understood it was because there was no provision as things stood which would permit them to vary their computation of taxable income in the two years involved. That is the

principle, as you know, of the whole objection.

MR. COYNE: This is the view of the Department of National Revenue here?

MR. MALTBY: So I understand.

MR. COYNE: Then your suggestion in this field -- turning the page to paragraph 68 -- is that:

"Section 41 provide that the unused portion of a foreign tax credit may be carried over to the same taxation years as business losses, i.e., the immediately preceding year and the five next succeeding years."

Can you explain how you envisage this carry-forward or carry-back of these credits would work?

MR. MALTBY: To the extent that the taxable income in the foreign country is greater this year because of a difference in computation from the Canadians, the tax in the foreign country is going to be greater than the equivalent Canadian tax as it involves income from that foreign country, and part of the foreign tax is not going to be allowed as a credit because Canada has not collected the equivalent amount of tax. But in the succeeding year when it is the Canadian base that is the greater, the foreign tax is going to be less than the Canadian but, under present circumstances, only that amount of foreign tax is going to be allowed as credits. So in those two successive years the largest amount of tax -- in one case the foreign and in the next case the Canadian -- has been paid instead of the mean of the two.

Does that answer your question?

MR. COYNE: Yes, thank you, that is very clear.

Do these differences of the computation between countries resulting in certain elements of income being brought into account one year in one country and another year in another country -- are these years ever back to back or do circumstances ever arise when there might be a two or three or four year gap?

MR. MALTBY: Yes. I am thinking particularly of depreciation circumstances. It may spread over a number of years, but I would think that five years would be a very helpful carry-forward and would cover surely most instances.

MR. COYNE: This is your view? It is your view that this type of relief, although admittedly partial, would substantially resolve the difficulty?

MR. MALTBY: Yes.

MR. COYNE: Then in the following paragraph there is still another aspect of the same problem. You state at the bottom of the page:

> "It is recommended that the taxpayer be given the right to file an amended return and retain a refund in respect of a foreign tax claim when the foreign tax is paid after the time for filing notice of objection for the original amount has expired."

There again, I wonder if you would explain

the way this difficulty arises under the existing provisions.

MR. MALTBY: The Canadian taxpayer's Canadian return has been assessed and -- I am struggling for the word -- is outlawed by time when the foreign is reassessed or when the foreign is assessed in the first place, and the Canadian return cannot be reopened.

MR. COYNE: The Canadian company in this instance has filed its Canadian return, has named a certain foreign tax credit, has been assessed and presumably the tax credit has been allowed and the 90 days from the date of the assessment has been passed, and therefore there is no appeal on the part of the taxpayer. Then at a later date -- is this the circumstance of which you are speaking? -- the foreign tax is reassessed?

MR. MALTBY: Yes.

MR. CLENNETT: I think it is Section 57 with which we are concerned, the four years which are permitted for a refund. You have no problem as long as you are within that period, but I think Section 57, speaking from memory, provides that you can get a refund within four years from the year end not from the date of assessment. So, for example, this is 1964, the end of the fiscal year in 1964, and anything back from 1960 will have expired. If you get 1960 returns reassessed in some other country after that and you are called upon for additional payments, then you have no means of getting anything back for that.

MR. COYNE: I see it is really the delay in the assessment procedure, coupled with the four years in Section 57, that is the problem.

MR. CLENNETT: That is right.

MR. COYNE: Then on page 27, paragraph 70, you are speaking of taxes paid to local authorities as distinct from the national authorities in the countries in which Canadians are carrying on business. You point out that some of these taxes if they are levied on income can attract no relief as far as Canadian federal income tax is concerned. I suppose there are in these countries many local taxes of a non-income nature which, in the ordinary course of events, are allowed as a deductible expense. Is that true?

MR. CLENNETT: Generally speaking actually there is one particular case in point. It depends from country to country and some countries or municipalities will choose to levy a tax on real estate, business or volume of business, and in some jurisdictions they will levy on profits -- and the same tax for the same purpose, by and large. If they levy on profits, then it is not eligible as a deduction under the existing Act and regulations in Canada.

MR. COYNE: Your suggestion is that these local income taxes be allowed as a deductible expense, which I take it would only be partial relief from any double taxation that one might attribute to them.

I am wondering why you suggest that they be treated in this way rather than be eligible, say,

for tax credit in the same way as income taxes paid to the national authorities.

MR. CLENNETT: Perhaps for two reasons, one that our own thought is that they are comparable. You are paying them to a lower echelon form of government, and by and large they do not qualify for tax credit regardless of their nature. If you pay the municipality of Toronto a business tax that is an expense item, but the same payments to the municipality of Toronto which are going to be used for substantially the same purposes are treated differently, and it would seem to us that it should be no more favourably or less favourably treated.

THE CHAIRMAN: You do get a reduction in respect of a municipal tax payment?

MR. CLENNETT: Not if it is a tax on income.

MR. COYNE: I suppose the other feature, Mr. Clennett, is that these local taxes if levied on income are levied at modest rates?

MR. CLENNETT: That is right.

MR. COYNE: If they were heavy taxes and simply treated as deductible expenses you would have provided a proper relief?

MR. CLENNETT: It would depend on the level of federal taxes. If it were the high government, you would expect your committed tax credit, and you would still get it.

COMMISSIONER WALLS: You have the situation in some countries where the heaviest tax is collected at the lower level, which then

allots money to the national government, so the main taxing authority in some countries is the lower form of government, as we consider it?

MR. CLENNETT: This is possible. I do not think we are represented in any of them. I think it is that way in Switzerland.

THE CHAIRMAN: Yes, it is that way in Switzerland and a Canadian bank opened a branch in Switzerland when I happened to be there. I do not know how it happened. I do not remember.

MR. COYNE: Perhaps we could go on to two relatively small points that you raise in the succeeding sections. One is the fact that commissions paid on issue or selling of capital stock, or borrowing money, are not allowed as deductible expenses, although other expenses are allowed. Do you know why the Commission was not allowed in the first place when this was first introduced in 1955?

MR. MACHABEE: I do not know personally, but if I did so it would certainly place us in the position of knowing the reasoning behind it, and whether that reasoning was right or not. All we see now is the fact that it is not allowed, and the reasoning is therefore questioned.

MR. COYNE: Is it always the case, Mr. Machabee, that the commission when received by a salesman or a commission agent is income to him?

MR. MACHABEE: To my knowledge, yes,

because you are talking about brokers which make it their usual business, and because of this fact it is always taxable.

MR. COYNE: You see no problem of loopholes that might arise here where they might not be taxed either in the hands of the company issuing or of the salesman?

MR. MACHABEE: No, because they have to make a business of it.

MR. COYNE: Yes.

Then you have suggested with regard to capital cost allowances, and I think this is quite clear, because I want to raise one question with you in respect of the detail, although perhaps it is just a drafting detail -- looking at the top of page 28, you have recommended that Schedule B of the Capital Cost Allowance Regulations be amended so as to include in Clause 12 any property that is a tangible capital asset costing less than $100 and which is not included in any other class. I just put it to you, if you include the words "which is not included in any other class", you might in effect defeat the objective that you are seeking. Would you agree with me in that regard? This may involve purely a matter of legal drafts-manship and, if so, there is no need to pursue it. Surely what you are suggesting there is that anything which is a capital asset costing less than $100 should be in this special class and the mere fact that it is a piece of electrical equipment, otherwise

falling in class 4, should not disturb it?

MR. MACHABEE: That is right. The suggestion is that the class should be broad enough to apply whether they are existing or not.

MR. COYNE: Any tangible asset of this nominal value?

MR. MACHABEE: That is right.

MR. COYNE: Thank you.

Then we get to estate taxes, Mr. Chairman. I have one or two questions in this regard.

THE CHAIRMAN: I think we are ready to proceed.

MR. COYNE: In paragraph 75 you express a philosophy which has been stated to us before in connection with the imposition of death duties. In the second sentence you say:

> "It seems unjust that so little cognizance is taken of the part that the wife plays in making possible the accumulation of what is, in fact, a family estate."

I presume you are thinking of what is, I suppose, the typical example of a man who enjoys a happy married life and then predeceases his widow after 35 married life, and the suggestion is that the widow has played her part in the accumulation of the family wealth. I wonder whether this is, in fact, a proper test in the field of death duties any more than in the field of income tax as, for example, there are inevitable exceptions where the man's wife has pre-

deceased him and he marries again and then dies within two years. It is hard to say that the widow in that particular case had anything to do with the building up of the estate, or the case where an individual is separated from his wife. I think the same circumstances would apply. I simply put it to you that the real justification for these exemptions is, perhaps, a question of need on the part of the surviving spouse. If she has no other source of support than what is left to her by her husband, this would apply, in the same way I suggest we justify the married exemption for income tax purposes. Would you care to comment on this little exercise in philosophy?

MR. CLENNETT: I think you have covered the situation. I admit there is the fact there that the widow has possibly and probably in most cases contributed in part, yet it is certainly an immeasurable factor of degree. The real problem involves a matter of need and a matter of degree. Our thought preceding our suggestion was that we think the exemption should be and could be more generous without materially affecting the revenue to the Treasury.

MR. COYNE: You are making a specific recommendation with regard to the surviving widow's exemption?

MR. CLENNETT: Yes.

MR. CURRIE: If we removed the words "in making possible the accumulation of what is, in

fact, a family estate", is there any less virtue in the suggestion?

MR. COYNE: There is no substantial difference, Mr. Currie. I made no suggestion at all.

I have no other questions in respect of estate taxes.

THE CHAIRMAN: I have, and I take it some of the other Commissioners will have questions.

I am quite intrigued by this thought of providing exemptions for equity. I am wondering how hard you want to push that suggestion. Certainly it would be most effective if one provided an exemption up to $100,000 for equities and no exemption for real estate and everything else from the first dollar. This involves a nice question as to where the right balance is. If, as you suggest, there was another $50,000 exemption by way of equities, I am not sure that is going to affect the kind of people that you wish to encourage to buy equities because they may have enough exemption without coming to equities at all. If you want to get the lower income people into equities and, as you point out here by your schedules, are already in to some extent, it may be that the exemptions should be of a total of something like you suggest apart from equities, and then that should be broken down as between equities and other securities. If you simply put it on top, I

am not sure it will provide the right incentive to the people of whom you have spoken. Am I right in that regard?

MR. KEAVENEY: The impact of this, of course, would have to be studied and researched by reviewing the various estates that are left by Canadians to see where the balancing point should be. Of course, our suggestion is that this would be an incentive to Canadians to own a greater share of Canadian equities, and I think also would contribute to a greater awareness and sophistication on the part of Canadians toward this kind of investment. It may be that the mechanics, and I am quite sure this is true, will have to be looked at carefully in order to achieve the objective that is sponsored here.

THE CHAIRMAN: This is a most intriguing thought. You have not got any equally intriguing thoughts which can be applied to institutions? I notice their relative holdings of equities is pretty low. I do not think we have received many good suggestions to encourage them to increase their proportion of equities. Perhaps it would not work by taxation anyhow because there certainly are limits as to how far taxes will go.

COMMISSIONER WALLS: Do you think it would be equitable as between someone who invests $15,000 in property which might be of equal advantage in the development of Canada, and individuals who invest $50,000 in Canadian equities? Would it not be better to have a straight $100,000 exemption?

As far as the amount of revenue is concerned that we are collecting between $50,000 and $100,000, it is very nominal, and it seems to me it would create an advantage to one type of investment but work in quite a different way in respect of other types.

MR. KEAVENEY: We have attempted to place our emphasis on positive measures aimed generally in the direction of greater participation of Canadians in Canadian equities which we feel is a very important sphere which requires encouragement in Canada. I recognize the point you make, Mr. Walls, that there could be individuals who had made investments in real estate, for instance, which would be quite commendable, and I suggest that this certainly would be an aspect of the subject that requires study. I make the point again that the objective we had in making this proposal was directed toward the greater awareness by Canadians of the advantages of owning a share of Canadian corporations; and equity share of Canadian corporations.

COMMISSIONER WALLS: I was thinking particularly of the farmers, being a farmer myself, who really have sufficient investment in equities but invest considerably in the improvement of land which provides food, and it seems to me they are entitled to just as much consideration as anyone else.

MR. KEAVENEY: I quite agree with you,

Mr. Walls.

THE CHAIRMAN: I suppose I might say that a professional man investing his money in professional practice is entitled to a pretty fair consideration.

COMMISSIONER WALLS: He is also in the position of being able to buy equity that the farmer is not. However, we will not debate that.

COMMISSIONER GRANT: I feel like entering this discussion myself. I do not know just how much emphasis the Association places upon this particular suggestion. I take it that it is really putting it forward more as a means of encouraging participation by the public generally in common stocks. If that can be achieved in some way it would be all right with the Association, but this is a suggestion which might be explored. The dangers have already been mentioned. The one that has occurred to me is that you would have a state of incorporations. Every person who is carrying on business today as an individual or a partnership would certainly wish to be incorporated and issue shares to themselves, or himself, if the shares were to be exempt. Now, if it were a case of listing and that was a qualification, a listing, of course, would have to pass the requirements of the Stock Exchange, in which case you might find that a person did not list his stock; he was in a very favourable position and would not, whereas the person who missed out on that qualification and

could not list his stock because he could not meet the requirements would lose. Therefore you would have discrimination within that class, which could create a good deal of dissatisfaction, I should think. You might make the requirement that a company would have to have at least ten shareholders, or something of that sort, so that a private individual could not incorporate for the purpose of getting this exemption. There again it becomes a question as to who these shareholders would be; whether they would have to be at arm's length or whether they could be within the family, and there again there would be more problems and more litigation if increased exemptions are to be given under the Estate Tax Act. We have to recognize, of course, that it is not by any means a major source of revenue at the present time, and to increase exemptions to the extent that have been suggested in the submission could very well result in the revenue disappearing to the extent where administrative costs would far exceed the benefits to be derived. These, of course, are matters which we possibly should consider in connection with the suggestion.

MR. KEAVENEY: I recognize the problems that would arise in developing some appropriate program to achieve the objective of the proposal which we have suggested. To us it is really part of the over-all package, if I might call it that, of ideas that we have come forward with in stimulating interest by Canadians in owning a greater share of Canadian equities. It is a

part of a program which calls for a reduction in the present tax structure and an increase in the dividend credit and, in addition, this possibly should have been examined in the light of the various estate taxes. This is really part of the whole idea that we are developing and proposing here.

MR. COYNE: Mr. Keaveney, I suppose you would point out in relation to any incentives to incorporate, such as has been mentioned, or in respect of even the question of discrimination against other types of property, that this would not arise in the case of small businesses, or a small estate, because below the level of the basic exemptions it would not matter whether a fellow had invested in real property or common stocks. These exemptions, as I understand it, would only take effect above the level of the basic exemptions which you are recommending?

MR. KEAVENEY: Yes.

COMMISSIONER GRANT: The problem there, Mr. Coyne, is that the estate is taxed as of the date of death. An individual always has great hopes as to what he may accomplish in his lifetime. He does not at the age of 50 know what his estate is going to be when he is 70. He cannot take a chance of not incorporating because he may find that at age 70 he has made a great mistake by foregoing that. That is, his estate may find that, because he is no longer there.

THE CHAIRMAN: There are obvious difficulties, but there are difficulties in regard to suggestions in respect of taxation generally. I think this is an intriguing suggestion and I assure you it will not be overlooked.

COMMISSIONER BEAUVAIS: On page 30, section 70, you suggest a survivor's pension could be levied on the pension actually received, but I presume that you mean whatever is in excess of the exemption. Supposing that the capitalized value is $75,000, you have suggested it should be taxed just on the $15,000?

MR. CLENNETT: Yes, that is right. It would have to be prorated depending on whether there were other assets, allowing for exemptions and so on. However, the problem that disturbs us is the fact that where the main asset is a pension, with very little cash, the money under present regulations and legislation is to be paid in tax at the time when the need is greatest instead of being spread over.

COMMISSIONER BEAUVAIS: Thank you.

COMMISSIONER GRANT: Well, you do not suggest it in your brief, but I wonder whether Mr. Clennett would comment on some suggestions that have been made -- other suggestions made in respect of handling all payments on an annuity or pension? With your scheme, of course, that the assets be assessed, and that the estate duty

be determined and then payments should be commenced and would cease on the death of the annuitant, but other suggestions have been made that there should be an option provision whereby the annuitant can elect that the tax be paid over a period of a number of years, say ten years, and that the tax would be collected under your scheme at the source by instalment payments, but at the conclusion of the ten years then the tax would be discharged -- the tax liability would be discharged and if the annuitant lived another ten years, the remainder would be received without deduction.

MR. CLENNETT: Assuming that they are going to get the same amount in tax over the first ten years and for that reason we think our suggestion is preferable in that it is spread over a longer period of time. True, you are paying it forever and there might be administrative difficulties, but on the other hand you are considering periodic payments and someone has to send in a cheque monthly, quarterly or annually, in any event, and it might even be easier administratively to feel that you have got to make a deduction for every payment rather than having to collect for each one when it matures and then knowing you do not have to deduct for that one any longer but that this is going to occur every month. We feel that on the basis of a deduction at source type of thing, this would be the easiest to deal with administratively, and at

the same time be the fairest way to the beneficiaries.

COMMISSIONER GRANT: The alternate course is that the annuitant might say: I do not want to be saddled with these payments the rest of my life, but would rather take care of them, and may have the resources to do so. The objection you are presenting in respect of the system arises largely because of the fact that if the annuity or pension constitutes the major part of the assets of an estate, then the duty that is payable on that may be beyond the means of the beneficiary to meet out of other assets. Now, if the situation is reversed and there are ample assets to meet the duty, should not the person be given the privilege of paying it either in a lump sum or over a period of, say, ten years?

MR. CURRIE: If I may just interject, we would agree with that completely. This has only presented one side.

COMMISSIONER GRANT: Yes.

MR. CURRIE: An alternative such as you have suggested would actually add to what we are suggesting here.

COMMISSIONER GRANT: Yes. You do not hang your hat on this entirely?

MR. CURRIE: Certainly not. I am sorry that that impression was given. We were not thinking of specific.

COMMISSIONER GRANT: I do not say that impression was given, but I thought it better to explore

all these views while we had you here.

MR. COYNE: Mr. Chairman, the final and following section of the brief is really the answers of the Association to specific questions directed to it by the staff. I only have one or two small relatively minor questions arising out of this material. Perhaps I should proceed with these and then if the Commissioners have any questions they can ask them afterwards.

THE CHAIRMAN: Yes, perhaps we might have a few questions later.

MR. COYNE: First of all, on pages 33 and 34 you are commenting in respect of certain peculiarities that perhaps arise as a result of Canadian taxation on foreign income which is derived from stocks and bonds which are taxed in a legal jurisdiction where, because of their tax-free features, usually produce a cash yield higher than would otherwise be the case.

In the middle of the page you say:

"Canadian banks, therefore, are operating at a disadvantage in that they have a heavier levy on their profits as compared with competitor banks as a resident in the country or from any other country which gives a tax preference to this type of income."

My question is simply whether or not you are making any recommendations for alleviating this difficult situation. I do not think you are. I think this is just something you live with.

MR. CURRIE: This is in the general context of the question on 82, but it does elaborate a little but there is no recommendation.

MR. COYNE: Thank you, Mr. Currie.

Then I just have one general question on the matter of reserves, and of course this question was raised because of the provisions of Section 11, subsection 4 of the Income Tax Act, and this is the context which is of interest to the Commission.

Are we speaking here as far as the Income Tax Act is concerned of maximum reserves or minimum reserves or prescribed reserves? As I read the Income Tax Act, subsection 4 of Section 11 simply states the maximum amount of reserve a bank would be permitted to take into the computation of taxable income. Is that correct?

MR. CURRIE: That is correct.

MR. COYNE: I suppose there is nothing that necessarily prevents a bank, if they choose to do so, from taking these funds and allocating them to any reserve as the management would see fit.

MR. CURRIE: I think it would work the other way around.

MR. COYNE: Then on the question that was raised about the deduction of taxes at source, which you discuss at some length, you distinguish between the difficulties that might be encountered in the disbursements of interest on the one hand, and interest. In paragraph 105 you say:

"To extend this type of tax to include resident shareholders would increase the volume of work and accordingly add to the costs involved in the disbursement of dividends, although the additional costs would not likely be unreasonably high."

I suppose one of the reasons for this is that each company paying dividends would have its own problems of applying withholding tax to the payment of dividends which it was making to its shareholders.

MR. CURRIE: Canadians?

MR. COYNE: Canadians.

MR. CURRIE: You are in a very large area here. Supposing this was a computerized operation, it would be practically nil. If the same

company was still doing business in an old fashioned way, the problem is a very considerable one.

MR. COYNE: I am leading up to this, Mr. Currie. You then go on to the very different scale of difficulties which, in your judgment, would arise if there was to be imposed withholding tax on payment of interest either through interest coupons or interest paid by the banks and other institutions on savings deposits. You point this out very clearly on page 43 in paragraph 109.

Leaving aside the question of savings deposits, which one might consider as being quite a separate problem, would you agree that the difference between amount of work involved in imposing a withholding tax on dividends on the one hand ---

MR. CURRIE: These are the bank dividends of which you are speaking now?

MR. COYNE: No, we are speaking I think generally here. A hypothetical question has been raised as to the complexities and difficulties of an administrative nature which might be occasioned if there was a general withholding tax on investment income derived from sources in Canada going to Canadians.

In commenting on this in relation to the payment of dividends in paragraph 105, you have taken the position that the additional costs would not likely be unreasonably high, but then in dealing with the problem of interest coupons and personal savings accounts you point out that the problem is

one of very different magnitude indeed.

MR. CURRIE: Yes.

MR. COYNE: The proposition I want to put to you is this, that leaving aside personal savings deposits of all kinds, and just taking up the question of a withholding tax on interest, on bonds and the like, is the difference not really that in the case of dividends the added cost would spread among all the companies who paid dividends to their shareholders and therefore would be very broadly spread, whereas in the case of interest coupons virtually the whole of the cost or a very large part of the cost would be imposed on the chartered banks because they are the cashing agents for most of these payments?

MR. CURRIE: Yes.

MR. COYNE: On the other hand, taking the question whether the over-all costs, by whomever they may be borne, is there necessarily any more of a cost to impose withholding tax on interest coupons than imposing withholding tax on dividends.

MR. SAUNDERS: When you speak of dividends and interest bonds paid by cheque, the routine is very simple in that withholding tax is paid by the issuer in that case. In the case of a bond of the Government of Canada it is very simple. In the case of coupons, they come in odd amounts and they have to be handed across the counter and the teller has to either have the customer make the

calculation or else do the job herself, and that is why your time builds up and the cost will build up.

MR. COYNE: I can see, Mr. Saunders, that it will be a very real and severe problem for the banks, a problem for which they might well expect adequate and proper compensation, but I am suggesting that the real difference in cost is that a very large section of the cost in respect of interest coupons is imposed on the banks because they in fact cash them, whereas in the case of dividends the cost is spread over all the companies which pay dividends to the shareholders.

MR. SAUNDERS: You have two parts to your question. You say the burden is on the bank as far as coupons are concerned, but apart from that the actual mechanics of making the calculations are much heavier with regard to the coupon no matter who does it than with regard to the cheques.

MR. COYNE: I think this is very interesting. Why would this be so as compared, say, with dividend payments?

MR. SAUNDERS: The calculation of dividend payments is made by the issuer, and the banks and big companies have computers now; it is just a matter of programming it. A lot of dividends are controlled by trust companies, and again they have I.B.M. systems. The smaller ones have a smaller volume. Again, on issuing cheques, you have a cheque register and you have valuation right down the page. However, the issue of coupons is

a random operation.

MR. COYNE: Which all 500 branches have to perform to some extent.

MR. SAUNDERS: Yes, and at odd times as the people come to the wicket.

THE CHAIRMAN: When one cashes a coupon there is an ownership certificate, and I am sure that is a troublesome matter for the banks. Would there be much difference between the handling of ownership certificates and making a deduction?

MR. SAUNDERS: Mr. Carter, it is a question of the calculation of the odd amounts that have to be worked out that takes time at the teller's wicket.

MR. COYNE: Supposing it was not odd, supposing it was 10% -- there is no teller in the country who could not deduct 10%.

MR. SAUNDERS: It may be easier, but the amounts are still odd and they have to be worked out and put down on paper.

MR. BOYLES: There is another feature of this operation in respect of ownership certificates -- they are not required in smaller denominations, and that eliminates a lot of the problem. However, the suggested withholding tax will apply regardless of the amount. As you know, you have a colossal number of bonds issued in small denominations.

COMMISSIONER GRANT: It might be stipulated that Canada's coupons could only be taxed at a Bank of Canada office -- provided the regulation

did not permit the Bank of Canada to set up deposit costs!

MR. COYNE: You made the point, Mr. Boyles, that ownership certificates were only required over a certain denomination.

MR. BOYLES: Yes.

MR. COYNE: It was my understanding that it was only on a certain amount.

MR. BOYLES: Yes, $3.00.

THE CHAIRMAN: That raises an alternative to the deduction system, and that is increased reporting. It has been suggested to us by some witnesses that there is a good deal of tax not collected because reporting is in many cases not below $100.

MR. BOYLES: Yes, and interest.

THE CHAIRMAN: And bond interest too.

MR. BOYLES: On saving certificates.

THE CHAIRMAN: And savings accounts. Other countries have reduced that very substantially. The United States has it down to --

MR. BOYLES: $10.

THE CHAIRMAN: If that were imposed, what kind of trouble would that be to the banks? Have you thought about it? You must have. It would not make any difference to the ownership certificate because they are down to $3 anyhow.

MR. SAUNDERS: On dividends, the problem would be very small I would say because again it is highly mechanized. There would be a higher

volume of work certainly on savings interest. For one thing it is paid twice a year, and there would be a much higher volume of transactions. I am not quite clear what proportion is down in the under $10 group, but a very high proportion is in the under $100 group.

THE CHAIRMAN: So it would impose quite a burden on savings accounts?

MR. SAUNDERS: Yes.

COMMISSIONER GRANT: I do not see how you could deduct and remit, if that is the suggestion, any tax on savings accounts, how you could have a withholding tax on savings accounts. I do not see that myself, but the witnesses are the experts.

The impediment to me is that until that account is withdrawn it belongs to the customer. It is the customer's. When it is in the bank, it is the customer's, and when it is withdrawn, of course it is the customer's. Could a savings institution, except by very stringent legislation, be permitted to charge the tax against the interest and remit that tax? That would be at variance, entirely at variance with our system of remissions now in effect.

THE CHAIRMAN: The owner could assign.

MR. CLENNETT: We have the same thing in the case of non-resident accounts now. One could explore the interest to non-resident savings accounts, and we are required to withhold the tax; it

is 15%, as I recall.

COMMISSIONER GRANT: But are you actually obliged to withdraw the amount from the savings accounts and remit that to Ottawa?

MR. CLENNETT: If you are going to credit $100, you credit the account with $85 and you remit $15 to Ottawa. You do not put two entries through the client's account; it is just one entry to the client's account and at the end of the year you make out a tax form showing what has happened. I am not advocating that; we do it for savings accounts and I am just saying that it is done.

MR. COYNE: It is done now in the case of non-residents because of the provisions of section 186.

MR. CLENNETT: Yes.

THE CHAIRMAN: My next question goes to your reference in paragraph 97 to accepted accounting practice. I recall an accounting bulletin dealing with reserves against receivables and the banks were exempt from the effects of that. The accounting principle which was laid down in that bulletin was that the reserve must pertain to the account then outstanding; that is, for commercial purposes there should be no cyclical provision for reserves or there must be no long term provision. That bulletin still stands. However, again there was no attempt to bring the banks into that.

Therefore, I assume when you say

"accepted accounting practice" you mean accepted accounting practice for banks. Is that correct?

MR. KEAVENEY: That is correct. We feel the cyclical form of accounting is designed to facilitate the economic cycle with which the system of banking, by its very nature, is closely related.

THE CHAIRMAN: I would like to just fully recognize that there is a clear difference in the method of providing a reserve for banking institutions and commercial -- which there is in my view, and which there should be I think.

MR. CURRIE: Yes.

COMMISSIONER WALLS: I was wondering earlier when you were first strongly advocating that Canadians should switch all of their investments from debt investment to equity investment why the banks themselves do not increase their purchases because recently we were shown some statistics by a participant which would indicate that the percentage is almost nil that is held by the bank.

I do realize that on page 35 you give one reason why you do not invest in equities -- because they are not regularly marketable in the sense of being saleable at a price, and there are two things I would like to ask.

Surely there are quite a number of equities that would fall within the category of being marketable at a price without the chance of too great a fluctuation. Secondly, are there any other reasons why you do not invest in equities?

MR. CURRIE: Basically the reasons are those set down here. The banks have been concerned properly and necessarily to keep their position liquid and that their assets be realizable immediately.

Quite frankly, I cannot think of any other reason. If you are asking for a positive reason why we do not, I am afraid I cannot think of one.

THE CHAIRMAN: Most of the claims against the bank are in dollars certain;they are not in any way fluctuating. Therefore you have to have dollars certain.

MR. CURRIE: I would think the same philosophy as the insurance companies adopt extends to us.

COMMISSIONER WALLS: They carry a considerable amount of loans, though relatively small in comparison with other holdings.

Am I not right in saying that the banks hold 30% of their investment in mortgages and that they would not be any more liquid than a good common stock?

MR. CURRIE: The only mortgages the bank holds as such are the National Housing Act mortgages, and they are in a rather different category.

COMMISSIONER WALLS: You have a government guarantee.

MR. CURRIE: We have an insured

mortgage, but this insurance is not operable until default of payment.

This was done in 1954. The banks were called upon to play a part in the policy to construct housing, and this is the reason for which they were made authorized lenders under the National Housing Act of 1954.

The banks,as you know, have ceased to lend under the National Housing Act and on their balance sheets now they are wasting assets.

COMMISSIONER GRANT: There would be some provision in the Bank Act, would there not, in which there would be restrictions as to the type of investment which you can have? For instance, the Canadian and British Insurance Companies Act lays down quite stringent restrictions as to the type of investment in which those companies under that Act may indulge. Fifteen per cent is the limit to which they are permitted to hold equities; and another restriction is that they cannot hold more than 15% of the stock of any one company. I should think there would be similar restrictions in the Bank Act.

MR. BOYLES: I think one of the things of which we should take cognizance here is that one of the prime functions of the bank is to meet demands for loans, and beyond that the matter of the investment portfolio is really perhaps basically to provide the necessary liquidity. Indeed, as pointed out in the brief, that form of liquidity is found in

-13

things which are more readily marketable than large blocks of equities, and such investments are usually of a short term nature. I think you go back to the prime point; that is, that the main function of the bank is to meet demands for loans.

MR. CURRIE: The investment function is rather vital.

THE CHAIRMAN: No one has ever worked out a form of deposit with a built in protection as against inflation which would put you in the equity business quickly. I commend the thought to you.

MR. COYNE: I have no further questions, Mr. Chairman.

THE CHAIRMAN: This has been a most instructive morning indeed. You have given us a great deal of material that we will ponder and deal with appropriately. The replies to the questions you have furnished have been very much appreciated by our staff who drafted the questions, and I think you have immensely assisted the work of this Commission, for which we are all very grateful. Thank you.

MR. CURRIE: I would like to say that our party is very grateful for having had an opportunity to assist in this matter.

THE CHAIRMAN: We will adjourn now and stand over until 2:30.

--- Adjournment.

(PAGE NO. 8756 FOLLOWS)

SUBMISSION BY FRANK M. McMAHON.

APPEARANCES:

Mr. Frank M. McMahon

Mr. Edwin Copps

THE CHAIRMAN: Yes, Mr. Secretary.

THE SECRETARY: Mr. Chairman and the Commissioners. This afternoon you have before you a submission of Mr. Frank M. McMahon of Vancouver, British Columbia. Mr. McMahon is here to speak to his brief, and he has also his associate, whom he will introduce, with him. I would like to enter this brief into the record as Exhibit 327, Mr. Chairman.

--- EXHIBIT NO. 327: Submission by Frank M. McMahon.

THE CHAIRMAN: Thank you. Good day Mr. McMahon. We are glad to see you and it is very nice to have a private citizen appear before us to speak out by himself. We have had numerous organizations, something over 200. We have had some private citizens but not very many.

I must say that certainly private citizens who undertake this sort of thing are undertaking a very serious public job. In fact, he has gone beyond what one normally thinks of as his duty. I am very much impressed to have a private citizen's thoughts . As you probably have seen by the papers, we have had about half a dozen citizens who have come forth and

given us some startling statements and some very interesting ones indeed.

You are, I think, perhaps the first person who has come before us with an accounting for the results of a tax reduction. We have had many people suggesting tax reductions. In fact, I don't know of anybody who has not said that but I don't think we had anyone tell us just how many jobs they think it will result in and what it would do to the G.N.P. Up till now I had thought it was only econometricians who did this sort of thing, young groups of economists playing around with an I.B.M. machine. I am very pleased to have you appear before us today. We will have questions to put to you but before doing so is there anything you wish to say to us?

MR. McMAHON: Thank you very much, sir, for those very nice statements. I appreciate it very much.

I have come today, Mr. Chairman and Members of this Commission, to present this brief on the basis that it is a proposal of a tax cut for the great multitude of people who are in the lower income brackets to say $20,000; the lower and the middle income brackets and they represent the great majority of people that pay income tax. I feel that the people over the $20,000 category, generally speaking, are in a position to look after themselves and they someway or other get along but the other fellow who has had a lot of tax deductions over the years from his pay cheque and his various other benefits, the old age pension and so forth, I think it is in my opinion

due time that the fellow making the money in the lower tax bracket should have some more take home pay.

I know in our corporation, why, the only thing people generally look at is "Well, how much do I get to spend?"

I have not an awful lot to say. I made a note here to just -- I did want to thank you for this opportunity of appearing here. We have done a study on this project, not alone. I have always felt that tax reductions would be a good thing.

Of course, I do a lot of business, that is, our company does a lot of business with the United States. We borrow money down there. We do a lot of financing both in Canada and the United States. Of course, we all know in the United States today that under the Kennedy Program they are going to have more than likely tax reductions.

The stock market itself is reflecting this to some great extent. For instance, our markets in Canada over the last year -- its general average has gone up about seven per cent, six and a half to seven per cent and in the United States it has gone up over 20 per cent, which is three times as much as we have been able to accomplish.

Of course, we have all kinds of disturbances as far as Canadian economy is concerned, where people have attempted to put restrictions on money into the country and the Kennedy Equalization Tax that is now or will shortly be before Congress is another detriment to our doing business, I think, probably.

I think the result of being able to do this in three steps, a gamble we are taking the first year is approximately you will notice here -- our budgetary deficit forecast for this year of 1963-64 is $565 million. Our present figures here would indicate that personal income taxes that the government would not receive would be $121 million and the corporation taxes would be $91 million. That results in $777 million.

If we lose all of that, that is the worse position we would be in with our forecast. It gives us a chance. If it does not work, I think what it will result in is a greater business activity, more spending and probably will result in many more jobs. This is on the basis of rule of thumb. The situation that might result in the first year is about 35,000 new jobs. In due course it will represent maybe 160,000 or 170,000 new jobs if we can use the figures that we have tried to work with, so if it does not work, if it does not stimulate things, we have not stepped off very far. You can go on. The next year it has a further reduction and the next year a further reduction so in total at the end we have approximately a little under 20 per cent reduction income tax in those brackets and for corporations. I think, Mr. Chairman, and ladies and gentlemen, that summarizes my general thinking.

THE CHAIRMAN: Thank you very much. Don't bother standing unless you wish to do so. I think I have added up your figures and perhaps you did for

yourself, as being over a three year period tax cuts of about a billion dollars and the recovery of about half of that.

MR. McMAHON: Yes.

THE CHAIRMAN: Which, I suppose, has some resemblance relative to the U.S. situation where they are contemplating around an $11 billion tax cut.

MR. McMAHON: $11 billion.

THE CHAIRMAN: I don't know how much they expect to get back by increased activities. I would think quite a lot, would you not?

MR. McMAHON: Well, they think so. Anyone who has made a presentation down there to Congress they all believe they are going to get all of this and more back. That is their belief, that it will stimulate the economy to such an extent that as far as having a balanced budget is concerned, they are likely to come up with something better than a balanced budget.

They have cut back a little on some of the unnecessary defence expenditures and things of that kind. More than likely they are doing it on a two step basis.

THE CHAIRMAN: Quite so. Well now, is it your view that the surge of the U.S. market, as you have said which is 20 per cent against ours of seven per cent, is to some extent because of the proposed tax cuts? Has the stock market improved because of the proposed reduced income tax?

MR. McMAHON: I think it has but they are discounting it.

Actually I think the people I have talked to down there, the knowledgeable people, believe this proposed tax cut that has passed the House of Ways and Means Committee is going to stimulate business and it has stimulated, I believe, the stock market.

THE CHAIRMAN: I think somebody pointed out to us the other day that our equities on an average sell about 16 or 17 times earnings.

MR. McMAHON: Yes.

THE CHAIRMAN: In the States it is something like 19 to 20 times earnings which probably is the same thing you speak of.

MR. McMAHON: Yes, I think that is true.

THE CHAIRMAN: I wonder whether it is due to the tax cut or to other anticipated benefits to their economy.

MR. McMAHON: Well, many people think that a portion of it at least is due to the proposed tax cuts.

COMMISSIONER WALLS: Do you think that the stimulation will continue after the tax cuts have gone into effect or is this purely a reaction of the market? Will the momentum continue in regard to the stock market?

MR. McMAHON: I think it will because I think it is going to create prosperity and I think it will continue. I just believe that. It may not go in such great jumps as it has gone. We have had a very big movement on the market in one year. Possibly the time earnings basis are too high. There are some

stocks going down there at 40, 50 and 60 times earning ratio. They have their growth stock which seems to have a great future and of course, ours are selling at a lesser price and should be a better security right now.

COMMISSIONER WALLS: We have people who say that they think that we may be wiser -- we have had such a diversion of opinion in this matter and your brief is very interesting and very worth while but we have had people who think that it may be advisable for Canada, in as much as we have followed the United States in so much of our fiscal policy, that we would be better to let the United States carry out this experiment and see the full term and reaction before attempting it in Canada.

MR. McMAHON: Well, it may be so, but I just don't just quite agree with it because I think that we are so tied in with the economy of the United States -- I am strictly a Canadian myself but I believe that there should be a greater flow of money out of Canada into the United States stock and security, if they are made more attractive by reason of the tax cuts so our balance of payments may be a factor. They could conceivably be a factor.

Many of these investment councillors in Canada have been suggesting that every portfolio, investment portfolio, should include possibly 25 per cent American securities. Well, I don't like to see that happen. I would rather see the money kept at home and keep our balance of payments down if we can.

THE CHAIRMAN: Your proposal is to divide the tax cut level equally between the consumer and the companies or producers.

MR. McMAHON: Yes.

THE CHAIRMAN: This is always a nice matter of balance, whether one encourages people to spend more money and increase the consumption stream or on the other hand invest more money to provide better tools and facilities and to improve our competitive industrial position.

MR. McMAHON: Yes.

THE CHAIRMAN: I think as I read your submission here you have taken it about 50-50.

MR. McMAHON: Approximately.

THE CHAIRMAN: On the $20,000 income bracket down one half million and half a million for the rest. It seems to me your argument supports a reduction in income tax to a greater extent than for the other side. We generally ask people should they have a choice, whether they would believe that it is desirable to cut taxes on business first to encourage spending on business assets -- lots of people are all in favour of that, or on the other hand cut taxes on the consumers and increase the market for Canadian goods.

MR. McMAHON: Yes.

THE CHAIRMAN: We get various answers to that. Would you care to discuss those two at all?

MR. McMAHON: Well, I will try to. Of course, I think that one helps the other to such a

great extent. I think that if personal income tax is cut to such an extent that a man will step out and buy more goods or more products in the country or he might even invest in some of our equities and very few do, you see. Personal investment in stock in Canada is about one in ten and in the United States it is one in five.

THE CHAIRMAN: One in ten people in Canada have some stock.

MR. McMAHON: Yes and just about half of the United States. There are a great many people in the United States today in this category who own shares than we do in our country, although our bank deposits are up and our savings loans and Insurance Companies have lots of money in hand. Our people are saving money but they still are not investing. I don't know whether this would help them, give them the incentive to get out and buy some of our equities.

Income, of course, I think if you cut corporation taxes it is an incentive to buy stock, not one but all.

THE CHAIRMAN: You mean you think earnings will go up?

MR. McMAHON: Earnings will go up and there is a chance to pay better dividends and you would have a better tax position. You would be in a position also instead of going to the money markets all the time, if you are a little bit too robust you would have money yourself that you could borrow money at a lesser rate when you have a better looking balance

sheet.

I think the lack of expansion programs by these companies is because many times they have to go outside of the country in order to finance them.

THE CHAIRMAN: Mr. McMahon, I do not see why if one reduced taxes on a corporation you are going to bring many people in the ownership of corporations which are not there already.

Supposing we carried to the extreme limit and eliminated taxes on corporations. Their earnings, if you like, would then be double roughly.

MR. McMAHON: Yes.

THE CHAIRMAN: And their dividends probably likewise.

MR. McMAHON: Yes.

THE CHAIRMAN: What will happen is the stocks will go up.

MR. McMAHON: Yes.

THE CHAIRMAN: Somebody goes to appriase them, he will see the same dividend yield or the same price earnings ratio, I would think.

MR. McMAHON: Yes.

THE CHAIRMAN: Well now, is that going to encourage people to buy more stock.

MR. McMAHON: Well, I think certainly the earnings ratio or the times earning ratio you will be in a position -- yes, I believe it will.

THE CHAIRMAN: You think it will.

MR. McMAHON: Yes. I believe it will. I think it creates more credits for people in our

country. In other words if the stock, instead of selling at $10 is selling at $20, certainly you will have more money to borrow money on. You can sell that particular stock and buy another one in some growth situation but if your stocks are selling at a low figure, why you certainly have not the wealth you would have if they are selling at a higher figure.

THE CHAIRMAN: It would improve the wealth of the people who have stock.

MR. McMAHON: Yes.

THE CHAIRMAN: But the people with whom you are concerned are those in the lower level who are not buying stock very much because you speak of a relationship of ten to one against five to one.

MR. McMAHON: Yes.

THE CHAIRMAN: Therefore, I would say really when you speak of them, you are speaking of families that do not buy any shares at all.

MR. McMAHON: No.

THE CHAIRMAN: It doesn't make it any easier for them to buy shares.

MR. McMAHON: They have a little more money and there is a bit of incentive, I believe, if you give them the right incentive -- for some reason or other our people usually put money in savings accounts and they do not speculate or put any of their money intorisk capital to any great extent. I think they may be taught to by the right kind of people, people like Merril Lynch, for instance, who do a tremendous business with small accounts and

give great service in the United States. Of course, they are in Canada. I am not suggesting the Americans know better than we do but they do a very good job for the working man.

THE CHAIRMAN: We are very conscious of Merrill Lynch in the States, of course -- and, as you say, they are in Canada.

MR. McMAHON: Yes.

THE CHAIRMAN: But I do not think they have carried out the same propaganda or publicity in Canada as they seemed to have done in the States.

MR. McMAHON: No, I do not think so either. I do not think they are nearly as effective yet. I would hope some banking and brokerage concerns would attempt to get people interested in this in this country. I think it is important for people to have a share in the country.

COMMISSIONER WALLS: Mr. McMahon, we are already giving inducements they do not have in the States -- 20 per cent tax credit and with no capital gains. When you are quoting a comparison of five families against ten families, that is on a per capita basis. Is it not a fact that you have a much larger percentage of institutions investing in equities in the States than you have in Canada? Do insurance companies, in other words, not carry a bigger percentage of their investment in equities than they do in Canada? Is that not what raises the percentage in the United States?

MR. McMAHON: You see, the Metropolitan Life Insurance, for instance, do not buy equities, and many of the other big life insurance companies

in the United States do not go in for equities; they buy first mortgage bonds, government bonds, and so on. Then there are the pension funds, and there are other big funds, and there is a shortage of securities, actually. They have been buying many equities.

COMMISSIONER WALLS: That is why that percentage is so high?

MR. McMAHON: Yes.

COMMISSIONER PERRY: Mr. McMahon, there is one aspect of your proposal I would like to discuss.

It certainly is easy to conceive that a tax reduction would result in an increase in consumer spending. What I really would like to hear is whether you think this should be in addition to government expenditure or in lieu of government expenditure. In other words, should government expenditure be reduced by a corresponding amount?

MR. McMAHON: I would hope in due course we would be in a position to reduce government spending as a result of deriving income from some other source such as a better business atmosphere; I do not know. I would not want to make a statement that they should stop, because I do not think they can. In many areas the government is committed and probably they cannot always do what the present government is doing now, and that is cutting back on certain unnecessary, old-

fashioned defence situations which we have in the country.

COMMISSIONER PERRY: As you probably know, this is an argument that is raging still in the United States as to whether this tax reduction should be made without a corresponding reduction in government expenditures. I think the argument of the economists, and probably of those responsible for the program, is that what is needed is an addition to total expenditure. In other words, you have to leave government expenditure about as it is and in addition add a very substantial amount of consumer expenses, so that there will be no question of just reducing one as you are increasing the other. In an economic sense, a government expenditure has about the same effect as a consumer expenditure; it puts people to work and gives people incomes.

I think those who are really facing up frankly to the situation in the United States admit that what they really are seeking initially is an increase in the government deficit in the expectation that with increased economic activity the deficit will gradually be wiped out. You do not come quite down flat on one side or the other on this, although you do touch on it in paragraph 21.

MR. McMAHON: I do not suppose they will cut government expenditure in this country as in the United States, but they might cut certain things they are doing which are unnecessary and which

do not really produce any benefits as far as we are concerned. If you can stimulate the economy of this country so there are more jobs and better export situations for our goods we will become more competitive. I know the lumber business in British Columbia, as well as pulp and paper, is booming and it is in many other parts of Canada. We are exporting. These companies are all attempting to upgrade their plants and modernize buildings and build new buildings. Now, of course, that is the thing upon which I think the wealth of this country is based -- the production we can put out, consume, and sell in foreign areas. It may be that $7\frac{1}{2}$ per cent of our money is concerned so far as a competitive situation is concerned.

COMMISSIONER PERRY: I gather you are not frightened of the possibility of there being a government deficit for a while.

MR. McMAHON: I do not think so.

COMMISSIONER PERRY: The deficit would increase?

MR. McMAHON: It may increase in the first year; it may not. I think our gross national product is going to go up. I believe this might help it considerably. If it does, then I think we are going to derive a great deal of taxes and put people to work and therefore enlarge our plants and sell more goods outside of the country and to our own people. Our economy has to boom, I believe.

THE CHAIRMAN: You are on the side of

the economists, Mr. McMahon; they are the ones who tell us not to worry very much about the deficits or the national debts. The business interests are the ones who are generally coming forward and decrying deficits to us.

MR. McMAHON: Yes, I believe what we are doing and all the benefits the governments give people today are necessary and a good thing, and it has taken a lot of money to create these things -- hospitalization and various things that we have which are all very good. They are all very good and I think we can support these things, and particularly if we can upgrade our economy in some way or another.

COMMISSIONER GRANT: Mr. McMahon, as one with great experience in the financial life of this country, would you give an opinion as to where you would place the greater amount of emphasis if you had to raise money by way of the sales of common stocks or to raise money by way of the sale of funds. Where would you place the greatest emphasis? Where would you want the greatest source of supply to be?

MR. McMAHON: Of money for that purpose?

COMMISSIONER GRANT: Yes.

MR. McMAHON: So far on big projects it has been difficult to get one's money in Canada. I know banks, for instance, are precluded from making term loans.

COMMISSIONER GRANT: I mean in so far as the public are concerned, the Canadian public.

MR. McMAHON: I do not know how much you would be able to sell to the Canadian public if you got down to educating them and trying to sell them good securities. I should think you would be more likely to sell bonds in Canada.

COMMISSIONER GRANT: As an industrialist if you had to lose $5, $10 million, which would you rather do -- have a regular market for bonds or a regular market for equities?

MR. McMAHON: Generally speaking, from our Corporation's standpoint, if we can borrow the money we still have a reasonable equity position behind our borrowings -- 25, 30, 40 per cent. I prefer to borrow the money -- this is from my personal standpoint -- rather than diluting the company by issuing more common stocks, unless we had to do so.

If you have to do it, you may borrow to an extent and you may sell common stock to the other extent -- maybe 25 per cent common stock and 75 per cent bonds, first mortgage bonds, or second mortgage bonds.

I do not think I am answering your question.

COMMISSIONER GRANT: I think you are, yes. In paragraph 8 you say:

"--it is essential that corporate income taxes be reduced simultaneously with the proposed personal income tax reductions. At the present rate

> of corporate tax collection by the federal government, and with increasing levies of various kinds by provincial and local governments, Canadian corporations cannot retain sufficient earnings or attract necessary capital for growth and new development."

MR. McMAHON: Yes.

COMMISSIONER GRANT: And then in paragraph 14 you say:

> " If enacted simultaneously, the proposed personal and corporate income tax reductions will promote Canadian equity ownership by making it more attractive to Canadian investors."

So I am just wondering whether you, as an industrialist, if you were promoting a company or losing money in a company that is already in business, would offer the Canadian public equities, or whether you would offer them the opportunity to purchase bonds.

MR. McMAHON: From my standpoint I would say that we probably would want to offer both. I do not think it would be a good thing for us in our business to offer them equity completely. We would want to borrow. In our business we have to borrow large amounts of money, and we have to keep a certain percentage behind our debt.

THE CHAIRMAN: I understand your business is the pipe line business?

MR. McMAHON: Yes, pipe lining and also I am in the oil business -- pipe lining and some production.

THE CHAIRMAN: The pipe line is financed by debentures?

MR. McMAHON: We financed first mortgage bonds, 90 million bonds. The Sun Life and many other companies in Canada participated, but the largest participant was Metropolitan Life Insurance Company. Those are first mortgage bonds. Then we also marketed a so-called second mortgage bond which is subordinated to the first mortgage securities. We also sold a large amount of equities.

My personal view -- and I am not representing my company in this -- is that if we were to have a choice our preference would be to borrow what we could and still keep our equity correct percentagewise. So we would not say that we were going to sell equity or bonds, we would rather sell bonds to the percentage that we could.

COMMISSIONER GRANT: The equity participation you have offered in the Company has been by way of debentures?

MR. McMAHON: We have some convertible subordinated debentures, but we have sold common stocks straight, just common stocks. So we have something in the range of 6½ million shares of common

stocks and we have borrowed over $200 million for our plant. We are proposing now to enlarge this plant by another $60 million to $70 million worth this coming year, and we will borrow most of that. I know that money is not all going to come from Canada, because there is no one place from which we can get that amount in Canada and no one group of institutions from which we could borrow that amount. We will have to spread it in other parts of the world, particularly in the United States.

I am not sure that I am answering your question.

COMMISSIONER GRANT: Yes, I think you are.

When you go to the public with an offer of bonds or debentures, I suppose the success of that issue depends to a considerable extent upon the number of times over which your earnings will pay the dividend or the interest rate on that issue?

MR. McMAHON: Yes.

COMMISSIONER GRANT: That is a reason for which you would like to have more returning earnings in the company, or at least have more earnings in the company?

MR. McMAHON: Yes.

COMMISSIONER GRANT: So a tax reduction would be of more benefit in your particular case -- it varies from corporation to corporation, but in your particular case a tax reduction would improve

your prospects of raising your money through a fixed income type of security?

MR. McMAHON: Yes, I am sure it would and I do not think it only applies to our company; it applies to many others which are doing practically the same thing in the same business. Of course, Trans-Canada Pipe Lines are bigger than we are and of course they have borrowed a lot of money and have a lot of equities, and Trans-Mountain Pipe Lines and Inter-Provincial. The more robust position they are in financially, the better able they are to get money at lower interest rates. If you have a good solid company you can borrow your money -- and you gentlemen know; I am not telling you anything knew -- and you are in a better position than if you are in a borderline situation.

THE CHAIRMAN: Mr. McMahon, your suggested reduction in income taxes relates to those earning from $20,000 down. We have had a large number of people coming before us who would be pleased with $20,000 up, and they are mostly thinking of an improved climate for investments. They believe we want to get more equities in the hands of individuals and that we are only really going to get those from people who earn about $20,000 or more, that people below that income bracket are really going to spend almost all their money, and that anything left over will be used to pay off the mortgage on their houses, or will

be put to a pretty pedestrian use. Therefore they say that if taxes should be reduced, the reduction should come about from people who are able to invest because they will then invest more and will buy more equities. You do not subscribe to that?

MR. McMAHON: I am not striving to do that to start with. Naturally, I am thinking of myself personally, and I would be in a better position if my tax was cut; I never keep any money; It's put it to good use. I know I would do that and I know many other people would do it too. In due course, if they consider cutting taxes they may consider cutting some percentage off the higher income tax brackets. So then, I believe when you cut the corporation taxes, and make these companies sound investments and give them a better chance to pay dividends, the situation will be improved. Many of the people in the upper income brackets are stockholders and it is true that they are the people who buy stocks and who gamble, and they would certainly be making more and getting a better rate of return because their stocks would be worth more money on the market, and in that way, of course, you have more wealth. Those same people can then spend more money to buy more stocks and buy more equities -- because most of them do buy equities after they get their insurance paid up. So I am not against that, although I am not suggesting it; but one thing I do think is

it is more palatable to the government and to the people of Canada at this time to start in an easy way if we are going to do anything like this. We are showing here another couple of hundred million dollars that we will not be collecting by reason of these suggested tax cuts.

THE CHAIRMAN: It is a question of priorities. Some people choose one and some choose another. I think you have made the position very clear. It is perfectly understandable.

COMMISSIONER PERRY: I am wondering whether it would change the attitude toward bond financing if the large institutions were just as willing to take equities as they are to take bonds?

MR. MacMAHON: Of course it would help a lot in our economy if some of these very conservative institutions could be impressed into buying this equity. I know for a fact I have friends who would do business with a number of life insurance companies, and most of them generally speaking do not get involved in equities. Some accidentally may have bought a convertible bond of some kind and found in due course they had some stock. The reason they kept it was because it went up, and they made the best of it.

The banks generally speaking can only lend money on first mortgage securities, notes or inventories, whatever it is, as we all know. They are precluded from making terminal loans so they are not too flexible. They only lend money from day to day to businesses to produce working capital. I would like to see them do a great deal of buying in sound equities.

I think a good illustration of that is that some of the universities had big endowments years ago, and the men leaving the money to the universities stated that they could not invest in government securities. Twenty or thirty years have elapsed, the dollar has gone down in purchasing power and they still have dollars. Others bought equities. I know some of the bigger universities in the United States

such as Harvard, and some of the others who had good business managers, bought equities. They did not buy all equity, but instead of having $40 million they found out very quickly that they had $200 or $300 millions. They could have bought A.T. and T., or Consolidated Mining and Smelting, and in 20 years made money, and a lot of it.

COMMISSIONER GRANT: What concerns me, Mr. MacMahon, is when you talk about putting out common stock and the desirability of creating a favourable market for common stocks in Canada, is whether or not the owners of companies would be willing to lay the control of their companies on the line by issuing common stocks with voting rights. I am under the impression that that is quite jealously guarded and that today lots of companies could issue common stocks because the market is available to them. If you get a stock that is yielding you 3½ per cent today that is about equal to a bond which yields 5 per cent in so far as your personal tax is concerned. There are lots of stocks that are yielding 3½ per cent. There are any number of companies today that require financing, but if they can finance through the sale of a finance income type of security they seem to prefer to do that, and, therefore, they do not place the ownership or control of their company in jeopardy. Would you comment in that regard?

MR. MacMAHON: Of course. If I understood you correctly you are referring to a wholly owned subsidiary of some company that is operating

here which may be owned in the United States but which has no stock on the ---

COMMISSIONER GRANT: I am not talking about that at all. I am talking about a straight Canadian corporation.

MR. MacMAHON: Again I want to get this question right in my mind. What is your suggestion again?

COMMISSIONER GRANT: If they need to raise money and they want to go to the public for it then the first thing they do is go to an investment dealer and they tell him they want to raise $5 millions. He says to them: you have stock that is listed on the market which enjoys a good reputation; it is a popular stock with the investing public. On your present dividend it is yielding 3½ per cent on the market price. We can place an issue of this for you at such and such a price that will cost you $3.75 --- less than you can buy on a 6 per cent bond with your interest rate deductions. Or, alternatively, we can put out a bond issue for you for $5 millions because your earnings are such that we can show the public through a prospectus that you have earned your interest six times on this issue. We will have no trouble whatsoever in placing this bond issue for you. All right there is a favourable market for a common stock and you have already told us that a company will go to a finance income bond type of investment. Therefore I would like to know how favourable do you want to make the market for

common stocks?

MR. MacMAHON: I think that you do make them more favourable to common stocks if your income taxes are cut and you have more money in hand. I do not know just how to answer that question. Of course, the more favourable you can make it the more equity of ownership I believe we are going to have in Canada. If they were to go out, as you suggest, with either a bond issue or a sale of common stock, it is a matter of whether it would be in the best interest of the company to sell one or the other or both. I am not sure, because every situation is different. You are introducing this as an example and asking me what I would prefer to do, or what you think should be done.

COMMISSIONER GRANT: What do you think companies would do, that is my question.

MR. MacMAHON: I think they would govern themselves by the circumstances. They might say, we will go out with a five per cent preferred, or something of that kind, that could be converted to common, which is very popular. Many times that is the easiest way to get your money, and it also gives a man a certain amount of security -- five per cent on his money, and he also has the chance that in due course he will be able to go along with the growth of the company and trade these stocks, or convert them into a common group or a number of common shares.

I think the circumstances of every

company will differ. May be in some cases it would be much preferable to sell this equity and not be loaded with debt, because you are not loaded with any responsibility. Perhaps I should not put it that way, but certainly when you have a finance bond interest and the stock of your company is making money you pay a dividend. If the company is not making money you cut the dividend back and you are not under the same obligation. You are under an obligation to manage properly, but if business conditions are such that you are not making the money you are not up against the same obligations as you are in respect of a $5 million bond issue.

I do not know whether I am getting close to anything you have reference to, or answering your question, but I can just say, the more favourable you can make common stock or equity, the better chance we have of getting bigger participation in those companies in Canada.

THE CHAIRMAN: Thank you, Mr. McMahon. I don't think we have any more questions. We understand what you have put forth very clearly and it will be some little while before we get around to reporting it. In the meantime all this area will be explored by us and by our staff at some length. We are required to examine the effect of taxation. We are concerned to know what will happen if taxes are reduced what it does to the product of the country, to the income of the country and to unemployment and to the economic considerations and we certainly appreciate as has been very good for us indeed to have your views which is just a little different than anybody else's views that we have had so far. I suppose no two people are exactly alike but yours are liberal. They are good for us. Thank you very much indeed.

MR. McMAHON: Thank you, sir and I think the time that you people put in is a great thing for Canada. I think it is a great thing to do. I would like to know if we could add about a page to this as a sort of appendix that wouldn't make it too cumbersome which might give you further explanations of the way we think.

THE CHAIRMAN: Very glad to have you do that. Would you have enough copies to enter it into the record?

MR. McMAHON: We will have a number of copies in the next couple of days.

THE CHAIRMAN: Well, we close up on Friday. If you can do it before then, we will enter it into

the record in the usual manner.

MR. McMAHON: We will have it before Friday. It is only a page.

THE CHAIRMAN: Thank you very much. Is there anything Mr. Secretary?

THE SECRETARY: There are two things, Mr. Chairman. I would like to enter into the record a submission we have received from the Association of Professional Engineers in the Province of Ontario. This will be Exhibit 328. Also, Mr. Chairman, a submission that has been received from La Societe des Decarateurs Ensemblieres du Quebec; the Quebec Interior Decorators Association, which will be Exhibit 329. That is all.

--- EXHIBIT NO. 328: Brief of Association of the Professional Engineers of Ontario.

--- EXHIBIT NO. 329: Brief of La Societe des Decorateurs du Ensemblieres du Quebec.

THE CHAIRMAN: Tomorrow morning at 9:30.

--- Whereupon the hearing adjourned.

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SECRETARY

MR. G. L. BENNETT

INDEX TO EXHIBITS

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. 21

SUBMISSION OF THE RUBBER ASSOCIATION OF CANADA:

APPEARANCES:

Mr. J.W.H. Miner
Dr. R.V. Yohe
Mr. G.F. Plummer
Mr. K.E. Kennedy
MR. G.E. Smith

THE CHAIRMAN: Are you all assembled, Mr. Secretary?

THE SECRETARY: Yes, Mr. Chairman.

Mr. Chairman and Commissioners you will recall that on last May 23rd, I entered into the record as Exhibit 82 a submission sent in by the Rubber Association of Canada. This morning the Rubber Association representatives are here and Mr. J.W.H. Miner, President of the Association and the President of Miner Rubber Company, will speak to the brief and will introduce his colleagues.

THE CHAIRMAN: Thank you. Good morning Mr. Miner and gentlemen. Glad to see you and have you come up here today. When you sent your submission in before we read it with considerable interest and really hoped to have the opportunity of discussing it with you. I am very glad that you have afforded us that opportunity. We will have some questions but before we go to the questions were there some comments you wish to make?

MR. MINER: Thank you for your welcome,

Mr. Carter. I understand you have the record and dossier of those who are appearing with me. Perhaps I should identify them to you.

THE CHAIRMAN: I think that would be nice, if you did.

MR. MINER: On my immediate left we have Dr. Robert V. Yohe who is Vice-President of the Rubber Association of Canada and President of B.F. Goodrich of Canada Limited who are engaged in manufacturing of a very wide range of products through the rubber industry; tires, industrial products, foam and plastics. On my immediate right is Mr. George Plummer who is a Director of the Rubber Association of Canada and President of Dunlop of Canada Limited, whose firm is engaged in tires and a wide range of industrial products. On my extreme right is Mr. K.E. Kennedy, Secretary of the Goodyear Tire and Rubber Company of Canada Limited, who again is engaged in tires and industrial products and in shoe products and plastics. On my extreme left is Mr. Greg B. Smith, General Manager and Secretary of the Rubber Association of Canada. My name is John Miner, President of the Rubber Association of Canada and President of the Miner Company who are engaged in footwear and rubber clothing.

I think at this time, sir, we have very little to say except to perhaps refer again to the recommendations we made on page 11 of our brief.

"(1) That the percentages of total revenues collected through taxes

on corporate income tax and personal income tax be reduced and the percentage collected through sales tax correspondingly increased,

(2) That the sales tax be converted from a manufacturer's sales tax to a retail sales tax,

(3) That the retail sales tax apply to services as well as goods including imported goods, and

(4) That the exemptions from the sales tax be strictly limited to expenditures on basic necessities of life and producers' goods."

With one more comment, sir, the brief has been approved by the Rubber Association but if I may make a statement to avoid any thoughts that there might be dissension within our own ranks, certain firms would perhaps have further views that are not contained in the brief and with the full approval of the Rubber Association, we have told them if they wish to present those views they may do so and with that I think I will sit down.

THE CHAIRMAN: Thank you, Mr. Miner. When reading over your brief before I was quite impressed with the flow of this national trade in the rubber business. I was rather curious as to why imports continue to rise to $46 million in 1962. I think you have attached a schedule -- no, I am thinking of

somebody else.

MR. MINER: There is an appendix 2, sir.

COMMISSIONER WALLS: Appendix 2, Table 4.

THE CHAIRMAN: Thank you. Now, what would the imports consist of? You are speaking about manufactured goods, I believe.

MR. MINER: Yes.

THE CHAIRMAN: And would they be cars?

MR. SMITH: Yes. A very wide range of goods, sir. Tires in 1962 accounted for $11 million worth of total. Various types of footwear produced by the rubber industry accounted for about $8½ million. Industrial rubber belting $2¼ million and then a very wide range of miscellaneous products, heels, soles and soleing material, hot water bottles and nursing nipples, sundry rubber sheeting, gaskets and washers, mats and matting, weather stripping, rubber automotive parts, cement, golf balls, liquid sealing bonds, hard rubber strips, rubber flooring,foam rubber sheeting, rubber sheeting, others and then miscellaneous which in itself amounted to about $8 million.

THE CHAIRMAN: Thank you. Why would imports, against exchange, continue to increase. First of all, where do most of the imports come from? Tires, I suppose, come from the United States?

MR. SMITH: Mainly the United States, yes sir. And footwear, our chief source of imports are Japan, Hong Kong, India, Czechoslovakia, and the

Asiatic countries with low wage rates -- Communist countries where costs are, I don't think, affected by their selling price too much at all.

THE CHAIRMAN: Taking tires, which is the largest single classification. We can produce tires as cheaply as they can in the United States.

MR. SMITH: That, sir, I cannot speak on. Perhaps Dr. Yohe might answer that one.

MR. YOHE: If we can produce and not have changes in the length of the run, I would say basically we can produce tires at least with the present modern equipment as cheaply as they can be produced in the United States.

The difficulty in Canada lies in the fact that the market is small. We try to be all things to all people; therefore, we are producing a wide variety of tires which means a constant change within the manufacturing of operation scheduling, changing of models and changing of manufacturing specifications and so forth.

THE CHAIRMAN: It is the old story of the short runs.

MR. YOHE: That is part of the story, at least. There is another factor in the importation that has not been mentioned. The fact that many large tires are not manufactured in Canada at all and those must be imported. In other words, the market is so small that the insulation of expensive and very heavy equipment to make the large tractor tires of the road which you see on the Marda excavations and so

forth -- they are imported because the market here is not large enough to support the installation of the equipment used.

THE CHAIRMAN: I suppose imported automobiles come with the tires on, do they?

MR. YOHE: Yes.

THE CHAIRMAN: Does this count as an importation of tires?

MR. SMITH: I don't think so, sir. They are simply part of the automobile. These are replacement tires primarily.

COMMISSIONER WALLS: With respect to the rubber footwear that is imported, I suppose, it is mostly of a price and quality that you do not produce yourselves?

MR. MINER: Well, I would agree with you there it is the price that is very difficult for us to reach. As far as the quality is concerned with some importations the quality perhaps has been slightly less than normally manufactured in Canada. The quality of some of the imports is extremely good but the price factor is the big factor.

COMMISSIONER WALLS: It would only be the cheap shoes that use the imported rubber heels?

MR. MINER: Yes, that would be right.

THE CHAIRMAN: Turning to export you point out a decline from a high in 1948 down to about $11 million now. I would think that some of the production in this area must be as economic as anywhere. With our wealthy neighbours to the south, can we

export into that market?

MR. SMITH: We do, sir, and as a matter of fact the United States is our biggest export market and it has been in the past two years a growing market with the benefit of the lower value of the Canadian dollars.

THE CHAIRMAN: Your exports are moving up?

MR. SMITH: Yes sir. In 1961 and 1962 they moved up quite well and actually in 1963 for nine months they amounted to $11 million as compared with $11 million for the total twelve months of 1962. I have a statement here, sir, detailing the import and export trade. I would be glad to file it if it would be of interest to you, sir.

THE CHAIRMAN: Thank you very much indeed.

THE SECRETARY: I will attach this to the submission, Mr. Chairman.

THE CHAIRMAN: Now, going to taxes you draw attention particularly to the extent to which this country imposes direct taxation. You contrast that with direct taxation of other countries. We get all kinds of pictures in this area, depending on how they are classified. I think this is the U.N. classification you are using and possibly that is the best one to use although it certainly shows a greater extreme than I think I have seen before.

COMMISSIONER WALLS: I believe that the United Nations figure show both a customs tariff and also property tax in those figures.

THE CHAIRMAN: Which way?

COMMISSIONER WALLS: Well, if I am right in this, I am only basing it on past checking they show property tax and indirect taxes as well.

COMMISSIONER GRANT: This is limited to Central Governments in that group?

THE CHAIRMAN: Yes. I think most of the figures we see are of Central Governments put together to show the impact on the taxpayer. You are dealing only with the Federal Government in Canada and the Central Government elsewhere but you suggest if direct taxes were decreased as indirect were increased it would provide more funds for investment in industry and stimulate industry. The other side of that argument is that if one imposes taxes on consumption it will have a depressing effect on consumption. The domestic markets will tend to diminish and there is not much purpose in providing funds for facilities. Do you believe that the Canadian consumer can stand more sales tax without affecting their buying power.

MR. KENNEDY: Mr. Chairman, the answer to that is yes. We believe that the Canadian economy in the past has accepted higher rates of sales taxes. We suggest that other industrialized countries are currently accepting higher rates of sales tax. I think that the purchase tax of the U.K. although they are objecting strenuously to it it does show up a sales tax in a much higher level and therefore it is a matter of straight comparison,

we would think we would suggest that the maximum sales tax level has not yet been achieved.

THE CHAIRMAN: Well, Mr. Kennedy, if you are contrasting it with the U.K. you must remember that the U.K. purchase tax is the only sales tax. They do not have provinces.

MR. KENNEDY: Yes.

THE CHAIRMAN: Whereas if you have our two sales taxes together and combine the rate I think we probably have the highest sales tax rate of anyone around. It is generally thought the 11 per cent manufacturer's tax comes out to about eight per cent at the retail level and if you add three to five per cent you have between 11 and 13 per cent.

MR. YOHE: Do you consider it perfectly expedient to increase the sales tax at the consumer level?

THE CHAIRMAN: I will ask you that question in a minute. I am not here to answer questions, thank you.

It brings the total Canadian direct taxes up to a pretty high level and what I think you are saying to us is that even though it may be about 13 per cent, you think that possibly it can still go higher. We have not had many people tell us that. We have had a lot of people say that more revenues can be secured by widening the base to include services and things of that nature. We have wondered where the maximum level of retail sales tax might be because a lot of people have suggested that sales

-10

tax be placed on the consumer. I think the highest level on the consumer we have encountered is 11 per cent in Norway.

The taxes in France are higher but the spread is not on one level, but still you feel that the rate of taxes should go up.

MR. KENNEDY: Yes. We think, of course, also that the base should be broadened. I have probably been confused in regard to U.K. tax because I suppose the U.K. tax is a combination of sales tax and excise tax. I have been thinking, sir, in terms of comparing rates from the 45 per cent on the luxury goods, such as cosmetics and T.V. sets down to 25 per cent on consumer durables, household appliances and 15 per cent on confectionary and soft drinks and then 10 per cent on furniture and clothing areas. Possibly we had been diverted by that comparison. Another comparison you could make is the comparison on the excise tax that is presently in effect in the United States. Now, we appreciate there is no broad based sales tax in the United States but there is on a variety of articles an ad valorem tax of 10 per cent which are in addition to the local taxes and very specific taxes which range up to 20 per cent or more depending upon the impact of the specific tax on the price. Those appear to have been generally accepted although again this is only a vague recollection, but it seems to me that the excise tax in the United States was at a higher level, 15 or 20 per cent on various items, and then they

have come down again. Possibly they reached the point of less in return but we fell, of course, that the base could be broadened. We also suggest that the maximum has not been reached.

/64

I suppose the maximum is qualitative as well as quantitative. If the public were satisfied that they were getting good value for their money, if they feel that the government is good for them, why then I suppose the maximum or the ceiling would be higher than if they felt they were having poor government or no value for the money -- I don't know.

COMMISSIONER WALLS: If you have graduated tax that would take into consideration our present excise tax there would be no reason, based on today's tax that was carried forward, as you suggest, to retail level -- for it to be as high as the retail level would it? It would be if you increased the tax in line with your recommendations, but you suggest that the tax is 10 in some places and 15 in others. I presume if you carried that forward to the retail level it would reduce these taxes by 15 per cent to 11 per cent retail level to bring in about the same amount of tax revenue.

MR. KENNEDY: Then the sales tax would be reduced from 11 to about 7.

COMMISSIONER WALLS: To about 8.

MR. KENNEDY: Seven to eight, and then the total on the highest combination of sales tax and excise tax would be in the neighbourhood of 28 or 29 per cent.

COMMISSIONER WALLS: Yes, you are pretty close to the 30 per cent mark.

MR. KENNEDY: Which provides you -- and I am wondering if I understand the suggestion --

with a comparison with the highest taxes in the United Kingdom.

COMMISSIONER WALLS: That is right.

MR. KENNEDY: But we would have to add on, would we not, the provincial sales tax to arrive at the comparison?

COMMISSIONER WALLS: No. You were doing that, I understood. If you had eight per cent sales tax plus five per cent provincial tax, that is 13 per cent, and then your maximum of excise duty above that of another 11 would bring you up to a maximum of 24 per cent highest, including the provincial tax. Is that right?

MR. KENNEDY: Yes.

COMMISSIONER WALLS: Which would allow you some expansion up to 30 per cent maximum, as you suggest.

MR. KENNEDY: I did not suggest it but I will certainly accept it.

COMMISSIONER PERRY: Is the philosophy behind this sort of suggestion the fact that you can make this change without affecting industry and the business community at all in an unfavourable way?

MR. KENNEDY: You ask whether I am suggesting that we can move from a manufacturers' sales tax to a consumers' retail tax without adversely affecting industry?

COMMISSIONER PERRY: No, I was thinking of the more general approach here which is less direct taxation and more indirect.

THE CHAIRMAN: Your point No. 1.

COMMISSIONER PERRY: Is your feeling that you can have more indirect taxation without any perverse affect on industry?

MR. KENNEDY: Well, I would try to answer that by suggesting that any significant dislocation of tax is going to have a perverse as well as a beneficial effect during a transition period, and that might be quite significantly extended. We do not suggest that it would be feasible or practical to, for example, eliminate corporation taxes. We do suggest that a reduction of a reasonable number of points in the corporation taxes would have a long term beneficial effect.

I am perhaps a little out of my area with respect to this discussion, but I have always felt that there is a psychological difficulty that presents itself when any worker is asked to pay more than half of his receipts to his partner, his partner being in this instance the government. If I as a worker, either a person or a corporation, find that for my day's work I am not getting quite half of the fruits of my labour I think there is more than the usual deterrence to my ambition and my constructive activity in the community.

COMMISSIONER PERRY: These are quite valid arguments I grant you.

My fellow Commissioners are shortly going to get tired of hearing me asking this question: we do have the argument put forward by the economists

that this could be a very painful transitional period which might have the result of ending up with a higher general price structure than what we began with. The argument is that there is in any industrial country now a resistance to reducing prices; that you might take off a substantial corporation profits tax and have no effect on the price levels whatever. You then go to the indirect tax and load on a great additional burden, which just raises your general price structure that much more.

People in innocence have been speaking of taxing services. I am sure services are now a fairly substantial component in the cost of living index and would be immediately reflected in a change of the cost of living index -- and you know how sensitive unions are to this particular factor. So I think it has been a little too readily accepted that you can insulate the industrial operations from indirect higher taxes, and if you did not have compensating price changes you might well find that you have ended up with a generally higher cost structure.

This is unproven and it might in a very long period be that these changes would compensate, but I think there is food for thought in this line of argument.

MR. YOHE: This is a question of political expedience.

COMMISSIONER PERRY: No, it is just basic economics as to whether your price structure would not end up having built into it just simply the

addition of these indirect taxes which would affect cost and lessen your competitive export position.

MR. YOHE: This is true now with manufacturers' tax.

COMMISSIONER PERRY: It is true now.

THE CHAIRMAN: Your recommendation No. 1.

COMMISSIONER PERRY: The position in effect is stabilized now. At least you know relatively what the factors are.

MR. YOHE: That is not true in the tire business with the interpretation the Department of Revenue puts upon the law itself. We have four different tax collections for the tires we sell.

COMMISSIONER PERRY: Well let me ask you directly, as we have asked some other people, what effect it would have on your prices if the manufacturers' sales tax were removed from tires?

MR. YOHE: You mean as far as the price is concerned?

COMMISSIONER PERRY: Yes.

MR. YOHE: I would say it would probably lower the price.

COMMISSIONER PERRY: You see, it is the "probably" that is the cause for concern.

MR. YOHE: The cost for collection and the cost for accounting of all these are very significant. If we could eliminate those, then some of the costs would be taken right out of our operations and could immediately be reflected in the price.

THE CHAIRMAN: Would that go to the customer or to the shareholder?

MR. YOHE: It would go to the customer.

THE CHAIRMAN: You would not increase your profits as a result?

MR. YOHE: No.

MR. PLUMMER: I believe that the further back the tax goes in the process the more the price is affected because it affects the mark-up of each trader that touches it. There are traditional mark-ups in every industry. If there is a 20 per cent or 30 per cent mark-up at a wholesale level and 20 per cent at retail level he traditionally marks up the tax, and he must because he must finance it and have his bad debt losses against it. He must do each of these things. I believe if the tax were moved -- and I am not speaking of the question of reducing corporation tax but rather applying it at the retail level -- there would be an inevitable reduction in retail price.

THE CHAIRMAN: And a reduction in his profits?

MR. PLUMMER: There would be a reduction in his dollar profit.

THE CHAIRMAN: In his profits? I do not know what the dollar profits are.

MR. PLUMMER: He is more inclined to percentages than he is to dollars, by tradition.

COMMISSIONER PERRY: Why would he not just assume that he needs X dollars of profit to stay in business and that he is probably going to lose this

when the tax comes off and therefore has to find it in some other way?

MR. PLUMMER: It probably should, but the tradition in our industry is that he concerns himself with his percentages. Whether that would change, I do not know, but that is his tradition.

THE CHAIRMAN: We have had many people tell us this but they have not been very ready to say that it is going to result in lowered profits and obviously if there is pyramiding, it is a profit on a tax and if you take out the tax someone is going to lose the profit on the tax and the profit will disappear.

MR. PLUMMER: That is accepted and that is the tradition in our industry.

We always seek ways of cutting the price even before we have found the savings.

MR. YOHE: Mr. Miner mentioned that some of us might have separate ideas, ideas other than those concerned in the brief itself. This might be an appropriate place at which to make a point that I feel is significant. I am supporting the brief of the Association, but there is a further point I would like to make.

THE CHAIRMAN: May we come to that after we have finished with the points? Does this

bear on point No. 1?

I want to ask you as a corollary to Mr. Perry's question what would be the effect of a reduction in taxes on the business profits supposing five per cent were knocked off the corporation tax rate or 10 per cent were knocked off.

MR. PLUMMER: In our industry that would reduce the prices.

THE CHAIRMAN: It would reduce prices?

MR. PLUMMER: Yes, it would.

COMMISSIONER WALLS: I think you say that in paragraph 16 where you are dealing with corporation tax.

"If competition permits, corporations mark up prices to provide a profit 'after taxes'".

And I would assume that you are making a statement that is in confliction with some that we have heard. It seems to be an opinion that you are expressing here that is contrary to some that we have had from other manufacturing concerns.

MR. PLUMMER: In our industry I am sure it would --

COMMISSIONER WALLS: The corporation tax is invariably taken as a cost factor right through to the consumer?

MR. PLUMMER: Not in accounting.

THE CHAIRMAN: Would the reduced price operate quickly?

MR. PLUMMER: Immediately. In our industry anything has only to drop one half of one

per cent and it is reflected immediately.

THE CHAIRMAN: I can understand that, but this is a tax on the profits. If this was reduced, would it immediately be reflected in a reduction in price?

MR. PLUMMER: Yes.

COMMISSIONER PERRY: What Mr. Plummer is saying is that this is a very competitive industry.

THE CHAIRMAN: I am sorry, Mr. Yohe, I interrupted you.

MR. YOHE: I submit that the manufacturers' tax presently imposed is detrimental to the tire industry particularly; that it has created cost-price relationships that undermine the economic well-being of many tire manufacturers; and that unfair inter-company competitive circumstances have resulted from the present tax law and its interpretation by the Department of Revenue. This has resulted in the collection of four different levels of taxation, depending upon how the tire was sold, and this is highly unfair as I will bring out later.

I believe there is an equitable solution to this dilemma that is fiscally and politically acceptable, and one that puts all tire manufacturers on the same competitive basis. You have probably heard this recommendation, but I am suggesting that reiteration is not out of keeping with this meeting.

Since the present tax is on a fixed per cent, the point of application of this per cent becomes all important. Any marketer of tires who

buys them from an arms' length position with a manufacturer thus has a very great advantage. For example, the largest retailer of tires in Canada is not a producer. We believe he is a manufacturer as defined by the Excise Tax Act, and the tax he pays is imposed on his buying price, which buying price is essentially the manufacturing cost plus a profit by the manufacturer. It is only after paying the tax that the costs of advertising, distribution and other commercial costs, including profit by the retailer, are applied tax free.

This same situation holds for any private brand seller who is not a manufacturer. This same situation holds for one large, well-known tire company which has no tire manufacturing facility in Canada, but which buys tires under its brand name, from another company in Canada.

Tire manufacturers who market their own brand are thus at a very distinct disadvantage in tax application since the tax they pay is based on the final settlement to the wholesaler or retailer, as the case may be, and is hence a tax not on manufacturing but on selling price including all the commercial costs and profit which I have described.

I hold that it is these circumstances that have created unfair cost advantages for private brand sellers and have created the chaotic competitive circumstances in the industry. I suggest that continuation of these could lead to eventual possible failure of some companies and/or the elimination of

some of the consumer benefits that accrue from healthy competition.

I would be prolonging this meeting unduly by endeavouring to create a new approach to this situation, hence I merely wish to suggest that there is a very simple solution to this whole situation. It is my suggestion that the manufacturer's tax be so defined as to really what it is now called. It would be my thought that an appropriate tax be applied to "cost of sales" or "mill door costs" and that this tax be calculated from quarterly sales and income statements of each manufacturer. In fact, this method could be used to collect a tax from service industries as well, since all of these must provide statements from which income taxes are collected. The levels of tax would be determined by the needs of the government and would not necessarily be the present 11 per cent.

This suggestion has several advantages. It would make for simple and easily collectible tax under well defined rules. It would be much fairer to all classes of manufacturers and retailers. It would be politically expedient. It would not interfere with the taxing prerogatives of the federal and provincial governments. Further, it would create a potential cost reduction item for manufacturers because of the elimination of the vast accounting procedures now forced on the industry.

COMMISSIONER WALLS: Is one of the troubles about the variety of prices not because your industry has more discounts than most manufacturing

industries?

MR. YOHE: This may be true, but at present there is one tax paid on private brands and one on the wholesaler and another on sales to distributors who again then resell, and finally on sales to stores; and they are all different, so the same tire may be sold four different ways and different taxes collected on each one of them.

THE CHAIRMAN: Do any of you people wish to say anything on private brands?

COMMISSIONER WALLS: I was wondering whether Mr. Yohe is prepared to tell us what the final status is of the tire test case on private brands. It is your firm, is it not, that is concerned in the case that is now stalemated by the Supreme Court ruling?

MR. YOHE: We were involved but I do not know the full answer. Perhaps Mr. Kennedy can answer that.

MR. KENNEDY: I think I have had experience with what are known as the tire cases.

The tire cases were, as you suggest, stalemated as a result of a decision of the Supreme Court of Canada which, in brief, said that the Tariff Board had no jurisdiction to hear the appeal. The Tariff Board had asserted jurisdiction under section 57 of the Excise Tax Act and the effect of the government is really that the Tariff Board's appeal is limited to consideration of varying types of goods. After that -- and this occurred in 1956 -- the tire companies had no

effective way of getting to the courts, but quite recently the Turnbull Elevator case has been heard by the Exchequer Court and the decision resulting from that case has had the effect of expanding the definition of "manufacturer" in the Sales Tax and Excise Tax Acts and this judgment has not been appealed; it is, so far as we know, in the hands of the administration of the federal sales tax.

We have seen no emination of a change of policy.

COMMISSIONER WALLS: Am I not right, Mr. Kennedy, that you took your tire case to the Exchequer Court and the Supreme Court also ruled that they had no jurisdiction?

MR. KENNEDY: My recollection is that it was the appeal from the Tariff Board to the Exchequer Court which was in turn appealed to the Supreme Court of Canada.

COMMISSIONER WALLS: That is right, so the thing then stands as it did before?

MR. KENNEDY: That is right, sir.

THE CHAIRMAN: Would you like to comment on the recommendation of the Sales Tax Committee of 1956 on this subject?

MR. KENNEDY: Our recommendation at that time, sir, was somewhat similar to the recommendation that Dr. Yohe has just now presented to you. I think there is a good deal to be said for that suggestion. I think there is a good deal to be said for it in the context of the tire industry which is a highly competitive industry and which is gravely concerned about what we term to be the injustice of a private brand tax which is levied at the purchase price rather than at the first sale level of the private brand distributor, or as we describe him, the manufacturer.

Looking at it today and conceding that it is a solution to our problem as a general solution I can see that there are a number of undesirable

features. I think that as a general proposition it would have the effect of narrowing the base of the tax which in turn would have the effect of increasing the rate. I think also that the certainty of the tax is being damaged to a degree, because it would have to change regularly as manufacturing costs changed. It would seem to me then that you would have to somehow or other in every industry arrive at an average cost. People cost in quite different fashions.

Then, you would have an arbitrary dislocation of income tax in some industries which have a very high manufacturing content, and there would be a heavy levy, and on an industry that has a light manufacturing cost content and a high distribution cost content, it seems to me there would be a lighter levy.

We in the tire industry are somewhat prejudiced because of the great portion of our business that goes through the private brand manufacturers, and this colours our thoughts, we must admit. Since the private brands manufacturing is based on factory to our cost plus a profit, then it is only natural to suggest that standard brands should be charged the same tax. So, again to repeat, in our industry it seems to me that Dr. Yohe's suggestion is very desirable. For a broad application I can see that there would be a great many difficulties.

THE CHAIRMAN: Thank you.

COMMISSIONER WALLS: Suppose you move your tax forward to the retail level; how would you get by your problem of the private brand or special brand? You would have to do it by a system of uplifting of price, wouldn't you?

DR. YOHE: In respect of the private brand level, that is entirely correct. It would be more equitable. Either of the two suggested solutions could decrease the problem we have. One is to apply the tax at the final selling price and everybody then has the same level, or apply it at the mill grower level which accomplishes the same thing because it is uniform there.

THE CHAIRMAN: At the retail level, of course -- when we get to the retail level the consumer pays the proportion whether it is a private brand or not.

DR. YOHE: He pays it anyhow, whether he knows it or not.

MR. KENNEDY: May I say this, Mr. Walls, we do not object to a higher tax being paid on an article that has a higher price at the consumer level when it is competitive.

COMMISSIONER WALLS: I see.

THE CHAIRMAN: Except principally what we are trying to do is spread sales tax according to the amount of our consumption.

COMMISSIONER PERRY: I see that you have said yourself at page 8 of your brief, and I quote:

"--(it eliminates discrimination amongst the various forms and techniques of production and distribution.)"

It cures all your problems except the private brands will still continue to sell for lower prices?

MR. KENNEDY: Quite right.

COMMISSIONER PERRY: You do not argue on the ground of discrimination there?

DR. YOHE: This business was put on a competitive basis. If we want good distribution we have to be competitive.

COMMISSIONER WALLS: On top of page 6 you say:

" Sales taxes likewise raise selling prices but do not apply to goods for export and in the domestic market can be applied equally to Canadian and imported goods."

With respect to the words "--do not apply to goods for export", I realize your brief was prepared previous to the 1963 budget, but I am now interested in knowing to what extent taxes on machinery and production have prejudiced your price on export, or changes your ideas which are expounded in this paragraph?

MR. KENNEDY: Are you asking me, Mr. Walls?

MR. PLUMMER: I have a contrary opinion

to that of my colleagues and perhaps I should not speak first, but I do not believe that the tax on productive equipment is a very serious tax. Nor do I believe it to influence export prices. I think it is so small in relation to your total cost that any manufacturer that looks at that and is swayed in his policies is not being very realistic.

THE CHAIRMAN: What is the other side of opinion?

MR. KENNEDY: I shall be glad to express the other side's opinion. I do not think there is a difference, really, because I would subscribe to Mr. Plummer's representations, that the impact might in effect and from a practical point of view be very light. After all, it is 8 percent on a machine, and a machine is appreciated over five years, so you are talking about 20 per cent of 8 per cent on a machine which in turn is only a small element of the cost of the article.

THE CHAIRMAN: I thought the tax was 11 per cent?

MR. KENNEDY: It is to be 11, but it is 4 now.

COMMISSIONER WALLS: It will be 11?

MR. KENNEDY: Yes, it is 4, and then will be 8, and then 11. Of course the theory is, as I understand it, that the tax on machinery is an increase in cost, and just as any other increase in cost it has the effect of raising the price, and as it raises the price, then the price for the goods for export has the same prejudice as

the price for the goods for domestic consumption. Then in theory you are pricing yourself out of the market. I suppose the basic theory of the consumption or sales tax is that it is the man who uses it who pays the tax so to the extent that it appears in an increase in the price on goods for export it is injurious to our export trade, but whether that has any practical weight is another matter altogether, and I am inclined to agree with Mr. Plummer that it might be over-emphasized.

THE CHAIRMAN: You indicate that it has an effect on your price of goods for export, this 4 per cent, 8 per cent or 11 per cent, whatever it may be, but I gather from you that it is not such that should cause any damage to your export sales?

MR. PLUMMER: I do not feel that our brief is consistent if we are seeking a wider base sales tax and then later have a rather selfish variation from it. I think it is more important that we should press for this wider base because far too much of the -- I won't use the words "gross national product" remains untaxed today. I think the more that we can appeal for tax to be paid on, so much the better for the level of the cost of doing business.

THE CHAIRMAN: This, I might say, is most refreshing. We have been deluged by people saying the opposite.

MR. PLUMMER: Yes. We used to pay this tax. I do not think our costs were affected when it came off. I doubt whether they were affected very much when it went on again. I think we must recognize the need for funds. I do not think it is inequitable.

DR. YOHE: In answer to your comment, Dr. Carter, we talk a good game but do not practise a good one.

COMMISSIONER WALLS: I have a few questions. How far do you want to go along?

THE CHAIRMAN: I think we are at the bottom of page 6.

COMMISSIONER WALLS: I have some questions on page 6.

THE CHAIRMAN: Go ahead.

COMMISSIONER WALLS: I thought that a new point had been brought out here. I have been just reading some figures that would bear this out, that is where you say the sales taxes are neutral in this respect bearing with equal weight on the highly productive and the less productive enterprise. Should we take that in comparison with corporate income tax? We received just a week or so ago the last copy of the newsletter from the Canadian Chamber of Commerce, and it shows that over one-third of all corporations reporting to the government operate at a loss, so naturally that was over one-third of corporations which do not pay any corporate tax, but if they were

all in the manufacturing business or bearing tax say at the wholesale level, they would naturally all have to be paying sales tax, or their goods would have been paying sales tax.

THE CHAIRMAN: Their consumers.

COMMISSIONER WALLS: That is right. In the next paragraph you say this is particularly so for the individual whose investment income is subject to double taxation, and it looks to me as if you are perhaps ignoring the 20 per cent dividend credit there when you are talking about double taxation.

MR. KENNEDY: I would agree with that comment, sir. The 20 per cent dividend tax credit is intended to equalize and, except with respect to the very high grades, has performed that function.

THE CHAIRMAN: By your own statement, that probably performs it as well, because you have indicated to us that changes in income tax on corporations would be reflected in your selling price. Did I hear you say that earlier? If that is the case, that means that your customers are picking up the tab because it cannot be borne by both.

DR. YOHE: Well, the long run customer does anyhow.

THE CHAIRMAN: Some say one and some say the other. You apparently say that customers do.

MR. KENNEDY: Does it not vary with the

industry?

THE CHAIRMAN: It varies with the length of time. There are lots of variants.

MR. KENNEDY: Yes, it runs from black and white all the way through the spectrum.

COMMISSIONER PERRY: It is always dangerous to be dogmatic.

THE CHAIRMAN: You have got an answer for everything.

DR. YOHE: By this time you should have.

COMMISSIONER WALLS: That is all the questions I have in regard to page 6.

THE CHAIRMAN: I had a question to ask, but I cannot remember what it is. It is all right.

COMMISSIONER WALLS: Shall I go on to page 7?

THE CHAIRMAN: I would like to refer for a moment to professional services. Undoubtedly you have that marked. As a professional man I have personally no objection to it. It might be a good way of raising our revenue. I notice that most countries that tax services do not include professional services. It may be that these tax services are largely made up of professional people and they thus avoid this, I am not sure, but the argument against it is that the great proportion of professional services are absorbed in respect of producers' goods, and that this is an increase in cost rather than being a consumer tax.

That is said to be the reason it is left out. I would have thought that most professional people would not have cared less about this because it is going to be passed on in bills anyhow.

COMMISSIONER WALLS: The only thing I would say in that regard is that you emphasize services, yet when you deal with commodity taxes you are prepared to exempt basic necessities. Are they not basic necessities when you give services? In other words, what about doctors and medical bills, would you not perhaps have to get away from those, or services in that regard to the same extent you might get away from food on consumption tax?

MR. PLUMMER: I would think you would. Nevertheless, in the whole body of services there exists a great many that are almost luxury services, and those should be taxable. I should not think there would be any objection to certain basic essential services such as medical services.

COMMISSIONER WALLS: How would you feel if there was a tax on transportation including freight? How would that affect the number of products going to the seaboard?

MR. PLUMMER: I would support a tax on transportation. Again trying to be fair about the base of taxes.

THE CHAIRMAN: That is a very fair statement indeed.

THE CHAIRMAN: That is very fair indeed. The luxury services do not, we think, provide an awful lot of revenue by themselves unless you place the telephone in that category. I don't think you do. I think one would have to go to colour telephones; perhaps even interest, I don't know.

MR. PLUMMER: As being taxable?

THE CHAIRMAN: Yes.

MR. PLUMMER: I should think so. I have one comment on that point, that a great many professional services are incorporated in the cost of production already. That was much truer twenty years ago than it is today. I think the average individual uses professional services much more frequently right now than ever before.

THE CHAIRMAN: Yes, I think that is true.

COMMISSIONER WALLS: Continuing on: You deal with exemptions on consumption. You say that the exemptions from the sales tax be strictly limited to expenditures on basic necessities of life and producers' goods. Are you prepared to interpret for us what you would classify as being the basic necessities of life because we get that sort of phrase thrown at us quite often but nobody so far has been quite prepared to define what it means.

MR. PLUMMER: Britain has a basic necessity list -- I forget what you call it -- many commodities have been classed by certain types.

COMMISSIONER WALLS: They, I think, have gone much beyond what you are thinking about because

they have made a difference between all the other countries on the continent. They have gone to giving exemptions on refrigerators and things like that as basic necessities. I don't think you are envisaging anything like that.

MR. PLUMMER: I would not but the provincial taxes have now certain exemptions on children's clothing. I believe there is an exemption up to a certain age. You see mothers trying to get that small size so it is not taxable.

COMMISSIONER WALLS: We have also heard of the adult ladies who squeeze into size 14.

MR. PLUMMER: Bless them.

COMMISSIONER WALLS: You think children's clothing is a basic necessity?

MR. PLUMMER: Indeed.

THE CHAIRMAN: Up to a certain expenditure per child, I would have thought, it would be a necessity but there must be a great deal spent on children's clothing which could be frivolous. Would that not be true?

MR. PLUMMER: I think -- this is a personal view or a family view that the present size level is a not unfair one. I do not have any major objection to it.

COMMISSIONER WALLS: What do you think about drugs? Are they a basic necessity?

MR. PLUMMER: I think drugs on prescriptions are a basic necessity but I know it is a difficult list of rates to make but so are all taxing rates

difficult to make.

THE CHAIRMAN: What do you think about food?

MR. PLUMMER: Again I should think food should be an exempt product.

THE CHAIRMAN: Up to any limit? Surely my consumption and your consumption probably goes beyond the necessity.

MR. PLUMMER: Yes. I understand -- I cannot say this positively -- that in some of these countries which have basic food exemptions there are certain classes of food that are not exempt rather than defining what is taxable.

COMMISSIONER WALLS: The only point I am getting at is that: You say the present list has grown in a hap-hazard manner and when we start off going into these things, you see how difficult it is to know where you cut off necessities and the more you exempt then the more you are going to have to increase the total tax.

MR. PLUMMER: If it is written, there is at least certainty in it. The present taxing basis is a completely uncertain one in the application of sales tax. We don't know from one year to the next what our rate is. Our decisions are continually affected by what may or may not be a departmental ruling and it could not be more uncertain tax. We are rather hidden, if I may say so, unprotected. There is practically no body of law to help us or cases to help us on the application of sales tax.

It is all quiet, secret.

THE CHAIRMAN: If all rulings were published, would that help you.

MR. PLUMMER: I think if we could afford to put a man to get it, I think it would.

THE CHAIRMAN: If you could not, would it still help you if there were 14,000 of them?

MR. PLUMMER: Yes. At least we could seek advice somewhere. We have had our sales tax basis changed several times. The last base cost our industry probably $3 million a year. That was never passed on in the price. It costs our company almost $300,000. The difference was never passed on in price.

COMMISSIONER WALLS: Is your principal problem in this regard, that you are referring to processing materials. In other words we have only had a limited number of the processing materials classified. Is that where you are running into troubles with the materials used in the processing of your product.

MR. PLUMMER: That part of it is not too difficult for us. Our real problem is deciding what tax we must take on the finished product.

COMMISSIONER WALLS: Depending on the material that you are using.

MR. PLUMMER: Yes. When we sell a tire for $20 -- if we sell a tire to a service station dealer for $20, depending on who he buys it from, he pays exactly the same for it from one of our

wholesalers or one of our dealers or our stores and the tax could run all the way from $1.28 to $1.47 yet at the end it is exactly the same product. It is an equity of the tax so then we have to decide on each transaction which is the best way to sell it, what distribution bases and method can we avoid or use so we pay the least amount of tax.

THE CHAIRMAN: You mention producers goods in the exemption. I presume now we have got them down to raw materials virtually, have we?

MR. PLUMMER: Yes.

May I make a point about importation? In the reference to imports which you have queried at the beginning, we mentioned golf balls. I can speak of this first hand. We manufactured golf balls at one time. We had no wholesalers. It was a pretty marginal business. It was not too profitable. We found that we could import golf balls from our parent company and due to the fact that we paid sales tax at the importation level we made money whereas if we kept on selling these ourselves as manufacturers and paying at the dealer level, the difference was great enough to put us out of business.

COMMISSIONER WALLS: Did you bring them in in bulk and then package them?

MR. PLUMMER: No, we bought them in in boxes yet our costs were not really greatly different. The level of exemption of taxes at that time made the difference.

THE CHAIRMAN: Was that because the foreign

manufacture did not include certain costs that would have been included by a Canadian manufacture.

MR. PLUMMER: Yes. He had distributors; just happens to be a product for which he had distributors. We did not have distributors so we had no real basis for wholesale tax, that is a special rate, whereas he did, so it landed there at our factory much cheaper.

MR. MINER: May I add to that, sir. This is definitely a problem with footwear, the matter of dealing with importations on the question brought up before that we pay sales tax on the landed price where we have to pay sales tax for the accumulation of our factory costs plus warehousing, selling and distribution costs which means we pay a higher rate of tax on an equivalent shoe. This is a very definite disadvantage to us in the footwear business when we are competing with the Far East.

COMMISSIONER WALLS: Is that quite fair? He doesn't really pay it on his landed price. He pays it on the value for duty but that does not include the transportation cost from the country of origin; so it is not really landed duty.

MR. MINER: No, quite right.

COMMISSIONER WALLS: It would be fair if it was his landed price.

MR. MINER: It would still be to our disadvantage.

MR. PLUMMER: I might say there is a great laxity in the Customs Department in applying

their market value. It is a very difficult thing to determine the rate and a very easy rule to break and all of the responsibility for the detective work falls on the competitors.

THE CHAIRMAN: They are doing it all the time, are they not? Competitors are watching that their market value.

MR. PLUMMER: As best we can. You have to submit the price list of your competitor in the country that is doing the exporting which is not the easiest document to get a hold of.

COMMISSIONER WALLS: Your reasons for that is more against dumping in the tariff rather than any item of sales tax.

MR. PLUMMER: Yes, if there is dumping.

COMMISSIONER WALLS: With regard to the moving forward to the retail level and your strong suggestion that the adoption of a retail form of sales tax by the Federal Government could lead to a coordination of Federal and Provincial sales taxes which will reduce the total costs of collecting sales tax imposed by the two levels of government -- I think there is nothing wrong in what you say at all but I am just going to ask you to: Supposing the province had refused to coordinate, would you not then have two types of retail sales taxes and possibly conflicting regulations and exemptions which would make this almost administratively impossible for retail sales clerks to be capable of handling?

We have a lot of people who come forward

and say"Move it to the Retail Sales Tax Level and combine the two taxes." There is nothing wrong with that at all but let us suppose the provinces are not agreeable to doing that. You are still left with the fact you want a visual retail sales tax. If you do that and the provinces have one, are you not going to be in a worse mix-up in the sales tax than you are today?

MR. KENNEDY: We proceeded on the assumption that the competing government could be reconciled so far as our recommendations are concerned. We recognize they have a great deal of political difficulty naturally.

If your question is: Would we be content with two parallel systems of collection, we would certainly not be content because it seems to us to be a gross abuse of politics and we suggest that if the recommendation is sound in theory, our politicians are skillful enough in practice to be able to implement possibly our suggestion. We say that it would be best at least I think we say it would be best to have the existing machinery of a province used for the collection of the federal retail sales tax. In other words whatever point of tax may be in the province you would add the points of taxes of the federal government. That, to me, would have quite an attraction to the provincial government because they will be in control of the large field of taxation and parts of the political difficulty might well be that the central government, stripping

the provincial governments of control of the tax, pull them further apart.

There is another comment I would like to make on this phase of it. The retail sales tax has become a very important instrument of tax and it has become recognized as such by the provinces and if the central government maintains its present posture of collecting at the manufacture's level, introduced in 1920 when there was no attraction to sales tax, if it persists in its present posture within a reasonable length of time the provinces might have sufficiently covered the field that the federal government will in fact be hemmed in.

Getting back to Mr. Walls' question at what point does a sales tax -- what is the ceiling of a sales tax?

If the central government adheres to the manufacture's level and if the provinces exploit the retail tax, you will reach a stage where the ceiling will have been reached with the preponderance in the provincial collections and the opportunity of gaining more revenue by the central government will in effect have been closed off.

COMMISSIONER WALLS: Do you, using your same argument not fear the possibility that some of the provincial governments will recognize also that they are going to be forced to perhaps exploit the retail sales tax to a greater extent than they are using it today and therefore from that standpoint will not be at all anxious to see the federal

government invade a tax field which they have come to believe is peculiarly their own? In other words, is there not a possibility that if both governments get into that tax and it is a visual tax, because this is the next point in your brief, that the provincial governments being in the field already could very well become blamed within the consumers mind as being responsible for the whole retail tax and the provincial governments will be afraid of that.

MR. KENNEDY: That is a possibility, of course.

THE CHAIRMAN: What is your alternative? What is the next best thing?

You are certainly with the angels in trying to put the two together at the retail level. Everybody would like that, as far as we know.

MR. KENNEDY: Yes.

THE CHAIRMAN: Assuming it would not work for the reason Mr. Walls has given or for any other reason you care to make, what is the next best thing to do; leave it at the manufacturer's level and try to patch up the difficulties; move it to the wholesale level or put it on the retailer as an unseen tax of some kind? Those are the choices you have.

COMMISSIONER WALLS: That is a hidden tax at the retail level, a wholesale tax or a combination of both, of course.

MR. PLUMMER: A hidden tax at the retail presumably would be no change, merely an expansion

of the present tax. It would not be a retail tax as such if it were undisclosed.

I would think that starting from scratch with a manufacturer's tax and getting it into at least some body of law and body of ruling and so on that the Act could be understood and that the manufacturers or any business people could appreciate with their business and have a full knowledge of how much tax they are going to pay.

MR. KENNEDY: If I could not have perfection then it would seem to me that, because my principal concern is eliminating discrimination, the closer you get to the stage of perfection the less should be the amount of discrimination. Therefore I would recede from perfection and work downwards. In that respect, then, it would be the whole sāles tax where a large proportion of the tax would be collected on the actual price which gives us certainty and eliminates a good deal of the problems that beset our industry and undoubtedly others. And you would have to provide only discounting for the integrated wholesaler-retailer. So in answer to your question, failing perfection I would vote for the wholesale tax, the tax upon the price from the wholesaler to the retailer.

THE CHAIRMAN: It is only fair, I think, to note that this is your personal opinion and not that of your Association, which have not really discussed this.

MR. KENNEDY: Yes.

COMMISSIONER WALLS: But you would prefer the wholesale to the hidden retail tax which would be the next step down?

MR. KENNEDY: Yes, I would.

COMMISSIONER GRANT: I have just one question, and I do not want to explore this to any great extent.

I did understand Mr. Yohe to advocate,

as a means of simplifying administration, the tax being imposed at the manufacturers' level on total sales.

DR. YOHE: No, the cost of sales; take it right off the S and I statement.

COMMISSIONER GRANT: And is that included in the memorandum which you submit?

DR. YOHE: Yes.

THE CHAIRMAN: There are no more questions, I understand.

Thank you very much indeed for your submission and for appearing before us and helping us. We need all the help we can get, and you have certainly helped us.

MR. PLUMMER: May I make this as a plea in a general atmosphere of income taxes? In 1952 and 1953 I worked and lived in London, England, at which time I found a tremendously bullish attitude toward investment in Canada. I do not mean just in regard to my own company, but in regard to many others. I spent a great deal of my time trying to cool out some of the over-enthusiastic. Since then, over the last year, the atmosphere has greatly changed among these people and the degree of uncertainty of Canada's attitude towards foreign investment is, I think, quite a serious thing for our country.

I think that, rather than being critical of the foreign investors, as seems popular today, we should provide an atmosphere of welcome for invest-

ment because the sophisticated investors view uncertain taxes as critically as they do fiscatory capital taxes, and I think the more we can do as a country and the more the government can do to encourage rather than discourage foreign investment the better it is for our economy.

THE CHAIRMAN: Thank you. We have heard a good deal on this subject and I am very glad to have your remarks to add to those of other people. These are your personal remarks, I take it?

MR. PLUMMER: Yes.

MR. MINER: Mr. Chairman, just a few brief words to say how much we have appreciated the very pleasant welcome you have given us and the very pleasant informal way in which you have treated us. I think we have all enjoyed it and I think we would all like to wish the Commission success in the very difficult job you face.

--- Short recess.

SUBMISSION BY

THE SHOE MANUFACTURERS' ASSOCIATION OF CANADA

APPEARANCES

Mr. Eugene Henry

Mr. E. M. Sabiston

THE SECRETARY: The second submission this morning is to be presented by the Shoe Manufacturers' Association of Canada.

Mr. Eugene Henry, the Ottawa representative of the Association, and Mr. Eric Sabiston, a former President of the Association, now retired, was formerly President of the Perth Shoe Company, now the Brown Shoe Company.

I would like to enter this submission into the record as Exhibit 330.

--- EXHIBIT NO. 330: Submission by the Shoe Manufacturers' Association Of Canada.

THE CHAIRMAN: Thank you, Mr. Secretary.

Good morning, gentlemen. Thank you for the submission with which you have provided us and the views expressed in it. We have a few questions to put to you, but before we do so is there anything you would care to say to us?

MR. HENRY: Yes, Mr. Chairman.

We welcome the opportunity to appear

today, Mr. Sabiston and I, and we hope we can supply information or constructive suggestions that will assist you in the development of new long term tax policies for Canada.

Perhaps it would be helpful to identify the most significant aspect of our brief, and that is that it is the best possible document we have been able to write on behalf of our highly decentralized industry.

I personally welcome Mr. Sabiston's presence here today. He has had long and varied experience in the industry and, as a past president of the Association, the industry directors felt he was best equipped to speak on behalf of the wide range of opinions that is bound to prevail in such an industry as ours.

Unfortunately, our spokesman from Quebec was unable to attend today, but we will endeavour to speak on behalf of some of those aspects of the industry that centre in Quebec to the best of our ability.

THE CHAIRMAN: Thank you, Mr. Henry.

Some years ago I was associated with your industry because I was a leather administrator for Canada, and at that time I recall that substitutes were appearing. This was at the end of the war. I am glad to see you still refer to your business as leather footwear. I was going to ask you what you make footwear of now, but I presume you still make it out of the same old material. However, is it true

that we are moving more and more away from leather?

MR. SABISTON: I would say so. There are more synthetics being used in the shoe industry than ever before, but leather is still the principal raw material.

THE CHAIRMAN: Did I not see in the paper quite recently that some substitute now had the quality of breathing? I was never sure what that meant, but it was what one always spoke of the substitutes as lacking.

MR. SABISTON: That is the new product developed by Dupont Company in the States; they claim it has all the good qualities of leather, and none of the disadvantages, none of the poorer qualities. I am afraid our friends, the tanners, would not agree with that, but this product is being test marketed in the States. It has come out at a very high price, so at the moment it is not competitive with leather, but the time will come when it will be.

THE CHAIRMAN: So far as leather goes, would it not have to have a great deal better quality than leather to succeed leather, because leather is a by-product, and we will always have a supply of leather as long as we eat beef. I would have thought it was unprofitable to produce a counter-material unless it had much better qualities. Would that not be true?

MR. SABISTON: It remains to be seen whether the claims that they are making for this new material will actually be proven. If they are,

then through the law of supply and demand, if the demand for leather goes down and the supply increases, the prices of raw material will decrease to the point where there will be an adjustment. I do not think that development of Dupont will entirely take the place of leather. It is just like the other fibres which have been developed, such as nylon and dacron; they have not completely supplanted wool or cotton. They have made heavy inroads on those natural fibres, and I think possibly we can look forward to a similar development in synthetics as a substitute for leather.

MR. HENRY: As a development of your question, Mr. Carter, there is a reference to the rubber footwear industry on page 2 of the brief. Perhaps it might be well to develop a few comments for the record on this because unless there was mention of it in the submission that was presented before ours, an appreciation of the problems facing the footwear industry of Canada would have to encompass both the rubber and the leather footwear elements of it.

I listened closely to the questioning that went on with the group that appeared prior to us and there was only small reference to the footwear phase of their industry. If, however, there is something in their brief, background information and statistics and so on, we need not make any extensive remarks, but there should be something on the record of the Commission of how the common problems of the two elements of the industry,

particularly in the field of imports and the impact of foreign-made footwear of rubber.

THE CHAIRMAN: You have not seen their submission?

MR. HENRY: No, we have not seen it and I might mention that we deleted such references as I am making now from our brief because we felt it was an intrusion on their submission. But it is rather basic at the present time because we have, as we have pointed out in our brief, reached a plateau of production in Canada of about 48 million pairs, but there is this tremendous flow of rubber footwear from countries where it is very hard to find this value for duty that you were referring to today.

As far as the domestic market is concerned, you have what we might say is our production coupled with the production of the group that appeared prior to us today.

THE CHAIRMAN: Would you like some time later on -- not before us now -- to review a copy of their submission and then, if it does not take care of your interest on the rubber business, to write to us?

MR. HENRY: We would welcome that.

THE CHAIRMAN: You may support it or contradict it in any way you please.

MR. HENRY: We would welcome this opportunity because it has become quite involved. We have hinted at the problem. We can use as a good example the Bata organization that makes both

varieties in volume, and yet Bata remains what you might call a dominant figure in the leather manufacturing industry, and yet they are substnatial producers of rubber footwear, and they are just one.

THE CHAIRMAN: They produce in Canada?

MR. HENRY: Yes, they do.

THE CHAIRMAN: We would be very glad to have you do that if you would care to do so.

As far as you have heard your predecessors here, would you subscribe to most of what you heard?

MR. HENRY: Unfortunately we did not have the opportunity of reviewing the brief, but I think we would take exception to what I think were personal remarks made by the gentleman who was sitting second from the right. (Mr. Plummer) He took a rather cavalier attitude towards the tax on production machinery and I am afraid we would have to be repetitious. We are like so many of those who have appeared before you. We feel it is fundamentally wrong; it is wrong tax philosophy to put a tax there.

COMMISSIONER WALLS: May I cut in on this and mention machinery production, because there is a very interesting statement made at the bottom of page 5 which I think we should understand. There you say:

> "Even though shoe machinery is
> now available for purchase, nearly
> all Canadian leather footwear manu-

facturers rent their machinery."

Is this the only way you can obtain your machinery -- stick-on sole machinery, welting and lasting machinery -- because the firms who have the patent rights will only rent the machinery to you?

MR. SABISTON: No, sir. At one time what you said was true.

THE CHAIRMAN: The United Shoe Machinery Company was the company.

MR. SABISTON: The United Shoe Machinery Company are the dominant factor in the shoe machine business, not only in Canada but also in the States -- and in many European countries, but not to the extent of their dominance on this side of the water.

At one time, all the money you had in the world could not buy a machine outright from the United Shoe Machine Company. You could buy your sewing machines from Singer, but United always put their key machines on a basis of monthly rental and a royalty per pair of shoes. When the American government took the parent company to task for that and made them cease and made it compulsory that they offer their equipment either for rent or for outright purchase -- and that happened about seven or eight years ago -- the Canadian company changed and today any manufacturer who wants to buy equipment from the United Shoe Machinery Company can buy, but very few do so because the cost is so high and the amount of capital tied up is so large. There

again, in recent years there has been a very substantial increase in the rate of obsolescence in shoe machinery with the introduction of new methods, and I think I would be safe in saying -- and this is a guess on my part -- that from 80 to 90 per cent of all the heavy machinery used in shoe manufacturing is rented, exclusive of the light sewing machinery equipment.

COMMISSIONER WALLS: You rent this on a long term basis?

MR. SABISTON: Their leases used to be on a 10-year basis.

COMMISSIONER WALLS: That is why I am wondering why you are so worried about the proposed cancellation when the machinery is already on a long term lease basis.

MR. SABISTON: I am not sure about this because, as Mr. Bennett says, I have been out of the shoe business for two years, but I am given to understand that the United Shoe Machinery Company will now lease machinery, and that it has to make additional charges for installation and the sales tax on that equipment at the value placed on that equipment by the Sales Tax Division.

COMMISSIONER WALLS: You have already some machinery in your plants on a 10-year basis. You are not going to be taking on much new machinery for quite a few years yet, are you? The impact is not too great, is it?

MR. SABISTON: Not the initial impact,

but it is increasing every year owing to the rapid rate of obsolescence and the introduction of new equipment and new methods. I would say within that period the impact could be very serious.

MR. HENRY: I would like to clarify. Our prime concern in this particular field, I think, as with the last dies and patterns, which are not machinery.

MR. HENRY: I would like to clarify Mr. Walls' question. Our prime concern in this particular field I think is that lasts, dies and patterns are not machinery but are production equipment. So, as we have stressed in our brief, the hazards that remain in this industry are in the field of obsolescence or style changes. So that this matter of approaching lasts, dies and patterns on additional sales of footwear is a substantial element of cost, and this is in a particular area with which we are deeply concerned in respect of exemptions that were part of the June, 1963 budget.

COMMISSIONER WALLS: Your patterns were always considered as apparatus of the production rather than materials used in production?

MR. HENRY: That is right.

COMMISSIONER WALLS: I was wondering why -- have you ever made any attempt to have a different classification? It seems that your patterns might be considered as materials used in production.

MR. HENRY: We feel that they are. We feel there is a complete and basic difference of opinion between the industry and the present rulings of the National Revenue on this subject. We feel they are most unrealistic on that particular score. We feel that the June, 1963 approach to the problem was merely a search for revenue and it really does not, certainly in our industry,

make sense.

THE CHAIRMAN: Why "nearly"? It was certainly a search for revenue, and that is what the minister said.

MR. HENRY: We appreciate his problems, but once again it is our feeling that it is inconsistent with a real sound tax policy to find it there.

THE CHAIRMAN: I had thought I might ask you where one should seek the revenue in the alternative. The removal of this tax on production material would knock off some $140 millions in revenue. Where would one go to replace that? I suppose one could raise the sales tax one percentage point?

MR. HENRY: In principle I think that is the way. Once again I stress how difficult it is to speak on behalf of a group that has such a wide difference of opinion, but I would say generally speaking, we are so positive about the idea, tax is wrongly applied in its present location and that means to our people that it should be at the sales level. We have been consistent in this by joining with those others who feel that the tax should be over there.

THE CHAIRMAN: You have missed my point. What I am simply saying to you is, if you do as you propose, namely do not tax production facilities, would not certainly a reasonable alternative be to up the tax rate from 11 to 12 per cent?

One has to get the money somewhere. The Minister's last budget was faced, I suspect, with the need to raise more money.

MR. HENRY: Yes.

MR. SABISTON: In regard to lasts, dies and patterns, I think they could properly be considered as material which is consumed, you might say, in the manufacturing process. In the past, this was always considered as such, and almost in the same category as raw material which was not taxed. I think lasts, dies and patterns are entirely different from machinery.

COMMISSIONER WALLS: I think in respect of patterns I will agree with you, but your lasts I think are almost as long lasting, and I am saying that without a pun, as your machinery is. I am sure that some of your men's lasts in your factories you have had for many, many years, and it is only a matter of them wearing out that causes their replacement. I appreciate the fact that in respect of ladies shoes there are periodical changes in clothes, and so on, but your lasts are more a permanent factor, or almost as permanent a factor as your machinery.

MR. SABISTON: Mr. Walls, I beg to differ. At one time you were right, but not today. The obsolescence of lasts is a factor. In fact, any time that you are passing through the small town in which I live, Perth, about 50 miles from here, I would be very happy to have you come to my home and I will show you what happens to our lasts. They

are burned in the fireplace.

COMMISSIONER WALLS: You make high style ladies shoes?

MR. SABISTON: Yes, and even men's and children's today. What you just said about lasts, dies and patterns would have been absolutely true ten years ago, but since then, ever increasingly there has been a changeover in styles. This has been terrific, and this involves the lasts as well as heels; lasts, patterns, styles and dies. That item of cost has gone up considerably. The industry has had to do this in order to keep out, or keep imports at a minimum.

COMMISSIONER WALLS: Perhaps if you charged the sales tax as against firewood it would be equalized.

MR. HENRY: On that point, the samples that were brought to National Revenue of lasts would indicate that the very nature of the manufacturing process which is such, you see, that the leather is shaped around the last and tacked into it, and that the more it is used the sooner it ends up like this desk if it were filled with nails. Obsolescence is really difficult here and the turnover is terrific.

COMMISSIONER MILNE: I should like to ask a question and perhaps this might be a good time to do so. I am thinking of the alarming increased rate of importation which you have mentioned. I am not absolutely positive of the

division in this regard, but is there any one area in the shoe industry where the importation is of great significance? For instance, would it be in respect of women's shoes?

MR. HENRY: Yes, I would say the great volume of imported footwear, having regard to both the rubber industry and our industry, would refer to medium and low priced women's and children's and plastic varieties.

THE CHAIRMAN: That is because of style?

MR. HENRY: In certain cases it might be mostly because of the absence of style. In other words, if you go to Woolworth's or the Metropolitan Stores here in Ottawa today you will find children's canvass and rubber footwear selling at $1 and ten cents a pair, or $1 a pair, and they are coloured. It is basically the materials and styles which allow them to produce in great volume and sell in various countries including Canada. They have been able to attain volume production in that particular style.

COMMISSIONER WALLS: In respect of leather shoes, the greater volume being imported into Canada comes from Italy. I think you said the volume imported from the United States and the United Kingdom is declining and that the principal importation of leather shoes into Canada is from Italy.

MR. SABISTON: That is mainly due to the cost price and the low labour rate which prevails in Italy. It is due also to styling. There has been a trend toward substantially increased importation from Italy of men's shoes as well as women's, although England is still the principal supplier or manufacturer of men's shoes.

MR. HENRY: In regard to that question, Mr. Walls, once again the basic element in the industry in respect of importation is what we might call unregistered imports. That is, over a period of many years, those who travel, in the United States particularly, footwear and cosmetics and tobacco products are the three prime popular purchases, and not all of the footwear purchases are registered by any means. In fact, the industry feels that there is quite a large percentage of imports of footwear from the United States which are unregistered.

COMMISSIONER WALLS: I understand you want to move the sales tax forward at the retail level primarily because there is an opportunity for you to make someone else the tax collector instead of yourself?

MR. HENRY: I think it would be truthful to say that is one of the reasons, but in endeavouring to develop a consensus among those who are operating in the industry, I think that the feeling was, if we are searching for principles here, that the consumer should know how much of the net price is tax, and, if possible, it should be

visible at the time of purchase.

MR. SABISTON: Could I elaborate on that, Mr. Walls? The tax at the manufacturing level, say sales tax of $1 a pair which goes to the government on a pair of shoes selling at the factory level at $9 a pair, and 11 per cent is 99 cents, you see; when that gets to the consumer, the retailer gets his full mark-up on that and it becomes anywhere from $1.50 to $1.75 a pair.

COMMISSIONER WALLS: I have one further question in respect of something which may have quite a bearing in this regard. Your industry deals almost entirely, does it not, from the manufacturer right to the retailer? You do not deal through wholesale houses very much?

MR. SABISTON: The greater volume of business is done directly with the retail trade but there are still some very large substantial and successful shoe wholesalers in Canada.

THE CHAIRMAN: What are the names of those companies?

MR. SABISTON: J. A. Johnston of Brockville, you would know that company, Mr. Carter. The London Shoe Company in London and Lambert in Montreal. They are the leading ones but there are others. The percentage of business in the shoe industry done directly with the retailer is much greater today than it was 30 years ago.

THE CHAIRMAN: Would it be three-quarters of the trade?

MR. HENRY: What is the question?

THE CHAIRMAN: Would it be three-quarters of the trade that is done directly with the retail stores?

MR. SABISTON: I would say in fact it might be more than that.

MR. HENRY: I would be pleased to supplement our brief with brief details of the wholesale business.

THE CHAIRMAN: If you have the figures, fine.

COMMISSIONER WALLS: When you sell directly to the retailer am I right that the government has established now in the footwear business a 10 per cent adjustment in order to arrive at an equitable wholesale price?

MR. SABISTON: That is right. When a shoe manufacturer sells direct to the retailer at his regular established selling price the tax is 10 per cent. Now, if that price is changed to a buyer -- a chain store, for example -- that tax will go back to 11 per cent, depending upon the differential in the price.

COMMISSIONER WALLS: I have one question to ask, although I am departing from the subject of sales tax. You recommend a lowering of the tax rate, and this recommendation falls under the heading of Corporate Tax Policy, and I think you are speaking of the income tax rate in that connection?

MR. HENRY: That is right.

THE CHAIRMAN: What would be the effect on your prices or your profits if the corporate tax rate was lowered by, say, five percentage points?

MR. HENRY: I do not think there is any doubt about it, that it would be reflected in lower prices at once. We have, as we pointed out here, a highly decentralized industry, and intense competition prevails, so that in almost all instances a new rate would reflect a new lower price.

THE CHAIRMAN: You believe such a reduction would be passed on immediately?

MR. HENRY: I am certain of it.

MR. SABISTON: Mr. Carter, as you must know from your experience with the Wartime Prices Board, the shoe industry is an extremely competitive industry. What Mr. Henry has just said I believe to be true. The industry is very keen and business available is getting a little bit less which makes competition that much keener. I don't think there is any doubt about that.

THE CHAIRMAN: Of course, Mr. Sabiston, we are interested in knowing whether one's income tax is considered to be a cost or a division of profits. If it is purely a division of profits, I would have thought a tax reduction would go to the shareholders making no change whatsoever in the selling price. If it is regarded by your industry as a cost, of course, it would make a

difference in the selling price.

MR. SABISTON: Could I give you my personal experience?

THE CHAIRMAN: Yes.

MR. SABISTON: Personally, the way I have run my business, and it is no secret, income tax is always figured in, but we knew that we were liable for 50 per cent, or 40 per cent income tax and we would strive for a gross net profit on our sales dollar of at least 10 per cent, which would give us a net, after taxes, of 5 per cent.

THE CHAIRMAN: Thank you, that is a very helpful statement indeed. You do actually sit down with your accounts and figure out what is 10 per cent on the selling price after taxes?

MR. SABISTON: Yes.

THE CHAIRMAN: That is a very helpful statement, I think.

THE CHAIRMAN: That is a very helpful statement, I think.

I think we have got no further questions. Thank you very much, gentlemen, for your submission and for your help to us today. It is very good of you to come and see us, for taking the time and trouble. We appreciate it very much.

MR. SABISTON: May I say one more remark, Mr. Carter, before we retire?

THE CHAIRMAN: Yes.

MR. SABISTON: First of all, I want to express my appreciation for the privilege of coming here before this Commission. I was very glad when I read in the paper our government had finally implemented the various suggestions which have been given for a full investigation into the retail tax structure.

My own personal belief is that we have reached the point of stagnation in our tax problems and I was quite interested to see today and listen to the discussion with our friends from the rubber industry about the political implications of tax at the various political levels, the federal level and the provincial level, and I just thought of the poor taxpayer. There he is. They are all fighting over him. How much are they going to get out of him?

It seems to me, and I was very intrigued and I know you all must have read an article which

appeared recently in the Financial Post on this Transaction Tax about two or three weeks ago. I feel from my own personal experience that our taxation policy is something which has got more and more complex and to a large extent has had a stagnating effect.

If Canada as a whole is going to exist and to live economically in a world becoming more and more competitive, it would seem to me that we have got to put our house in order. In the first place, at the government levels -- I mean all the governments -- federal, provincial and otherwise, to cut down on these terrific deficits which we are incurring which is only leading to continued inflation and also putting some incentive where management, not only of industry, but of all businesses, will have a greater incentive to operate more efficiently.

I know, and you gentlemen must realize this, but very often we would fall into the habit of thinking "Well,"-- when we are considering an expenditure -- Well, what's the use. The government is paying half, let us go." That possibly comes into decisions more often than what we would care to admit and it would seem to me that if there were some way of changing the tax policy there in the first place to prevent this pyramiding of tax through increased mark-ups right down to the consumer, such as a sales tax -- $1 becomes $1.75, that the economists might be able to take our figures, our national product figures there and work out possibly another

method of raising money which is required to be raised and at the same time provide the necessary incentives. It might mean an adjustment in corporation tax. It may mean the elimination of corporation taxes and a reduction somewhat, not complete, on the income tax. I don't know. I know you have one awful job ahead of you trying to carry it out.

THE CHAIRMAN: Thank you, Mr. Sabiston. We have almost heard everything now. Nice to have seen you.

SUBMISSION BY

CEDA INCORPORATED

APPEARANCES

Mr. D. C. McKellar

Mr. J. F. Hoskin

THE CHAIRMAN: I think we are ready up here.

THE SECRETARY: Mr. Chairman and Commissioners. The next submission this morning is being presented by the Canadian Electrical Distributors Association. Mr. D. C. McKellar, General Manager of the Association together with Mr. J. F. Hoskin of the firm of Reiber, Hoskin, Shannon and MacGillivry are here this morning to speak to this brief.

I would like to enter it into the record as Exhibit No. 331.

--- EXHIBIT NO. 331: Brief presented by CEDA Incorporated.

THE CHAIRMAN: Thank you, Mr. Secretary.

Today Mr. McKellar and Mr. Hoskin, I am very glad to have you with us and thank you for what you have already furnished to us. You are, I suppose, connected with the wholesaler's Association -- I am sorry I cannot remember the exact name. They appeared before us within the last week or two weeks.

MR. McKELLAR: Yes sir.

THE CHAIRMAN: And they informed us that they

had various sections of different trades within their industry.

MR. McKELLAR: Yes.

THE CHAIRMAN: I think they made reference to the electrical wholesalers, and I presume you would come into their submission?

MR. McKELLAR: I don't think they mentioned electrical wholesalers.

THE CHAIRMAN: They did not?

MR. McKELLAR: Because we differ somewhat as a group.

THE CHAIRMAN: That is why I asked you that. I observed you did. You have given us a summary and you have given us the details of submissions, detailed submission on page 5, but I don't think you picked up everything which starts at page 1. Am I right? May I start at page 5, or should I start at page 1?

MR. HOSKIN: I think, Mr. Chairman, it would be just as well to start at page 5 because that gives the detailed account, in there from pages 5 to 9.

THE CHAIRMAN: I thought it did, and then I thought when I looked at page 1 that you did not. If we overlook anything by starting at page 5, please point it out to us.

You recommend a change in the level of tax to end-users or to retailers. That means that you would change this into a tax, I would assume, something like the provincial tax, or make

it a wholesaler's tax.

MR. HOSKIN: It would be a general wholesaler tax, Mr. Chairman, a tax where the product goes from the wholesaler to either the end-user or to the retailer.

THE CHAIRMAN: I thought you were offering us a choice, either the retail tax or a wholesale tax, but you are saying a wholesale tax.

MR. HOSKIN: Although there are some obstacles to it -- this tax certainly has one disadvantage and that is tax on inventory are still tied up at the wholesale level unless all so-called wholesalers were to be given a licence.

THE CHAIRMAN: You propose licences for wholesalers?

MR. HOSKIN: Yes.

THE CHAIRMAN: Of course then there would be no tax on wholesale inventories?

MR. HOSKIN: That is right.

THE CHAIRMAN: Retailers inventories would continue to carry tax?

MR. HOSKIN: Yes, that is right; in the electrical industry there is approximately 50 per cent of the manufacturers' goods that are sold through the manufacturer to the end user, so the manufacturer is a retailer then in that case.

THE CHAIRMAN: Quite so, and a large part would be sold from the manufacturer to the

retailer.

MR. McKELLAR: To the end-user.

THE CHAIRMAN: Would this mostly be through the wholesaler?

MR. McKELLAR: The wholesalers of the electrical industry in Canada do approximately 50 per cent of the total manufacturing sales.

THE CHAIRMAN: The other 50 per cent is to the consumer or to the end-user?

MR. McKELLAR: Yes.

THE CHAIRMAN: Which would be contractors?

MR. McKELLAR: No. The government or power companies or the telephone companies. Mostly engineering parts of their total volume.

COMMISSIONER WALLS: I am not entirely clear now as to this 50 per cent. You say 50 per cent is going through the regular wholesale channels?

MR. McKELLAR: Yes.

COMMISSIONER WALLS: Does that mean the other 50 per cent is being sold directly from the manufacturer to the end-user?

MR. McKELLAR: Yes, sir.

COMMISSIONER WALLS: Well, let me quote your own phrase: 'There is also the uncertainty that some competitors may be getting a better deal in the application of the sales tax base than others. In what way do you see that is going to be helped by having a wholesale tax or a manufacturer's tax? What about the large retailer who buys directly from the factory? Are you not in much the same

position of establishing an equitable notional wholesale price as you are today, either by an uplift or a discount? You are going to have to establish a fictitious wholesale price just exactly on the same basis that you have got to do it today.

MR. HOSKIN: No. The problem there, Mr. Walls, is that in the various wholesalers you have a different discount base on your re-constructed trade account and the members of this organization feel that -- all of them have not got the same opinion -- in other words there may be a deal where one manufacturer has allotted 90.9 per cent as a discount as a calculating base at which tax is calculated. The rate of practically everyone is different, because if you are a large trading account -- in this case we have one individual firm that is giving a high rebate on sales tax and the restricted trading account would not have the tax against that because a restricted trading account does not warrant it and in order to be competitive and to keep all customers happy, they have to go up to the rebate allotted by the person who allows the highest rate of tax rebate.

COMMISSIONER WALLS: What I am saying is: Would you not encounter that if you had a tax at the wholesale level?

MR. HOSKIN: Yes, we would. A tax at the wholesale level would not overcome that. Our suggestion to overcome that is that if there

were any special arrangements with a wholesaler or manufacturer in that particular trade that all other persons in that trade should have knowledge of it.

I mean, the Sales Tax Department has done a wonderful job in trying to level out all these various taxes, but we are in an industry that is highly competitive and one in which the licence holder has got a low marginal profit which cannot be maintained by the majority of the others in that industry. We think we should all have a chance to see what is what.

THE CHAIRMAN: Sorry to go back, but I would just like to see I fully understand just how your Association operates. You are the Canadian Electrical Distributors Association and you say in your introduction you represent distributors all across the country, and I suppose there are a large number of distributors, are there?

MR. McKELLAR: Well, we have about 70 members in our Association. There are approximately 250 other distributors, probably 15 of the 250 could join -- they would come within our by-laws. The other 230 odd they are fringe. They are handling several lines along with electrical equipment and the electrical part is a very small end of their business.

THE CHAIRMAN: When you prepared this submission, did you have a taxing committee, or is it an executive committee, or just how did you go about a thing like this?

MR. HOSKIN: What happened here, Mr. Chairman, is that our firm was asked to provide this submission, and we discussed the problems with the various members -- not all of them, but quite a number of representative members, and found out what their beefs were in connection with sales tax.

THE CHAIRMAN: The reason I am pressing a little bit on this point is that you are diametrically opposed to the wholesalers' recommendations in respect of changing the level of taxation. I was curious as to whether you had a very large number of your distributors with you on this.

MR. McKELLAR: Each one, sir, got a copy of our submission, and we had quite a number of replies; some criticisms, some corrections to be made, and others agreed with what we stated.

In regard to the wholesaler group, sir, they are dominated to a certain extent by the food industry and they did not wish any problems in that industry that are going to make it embarrassing.

We discussed this submission with them and they thought we were pretty good but they couldn't go along with us and we went along with them as far as the general brief was concerned but couldn't agree with all their submissions, and there is no question that competition in the food industry is pretty severe.

Tues.

To me it is just astounding how they can carry on business. A number of grocery people send in a blank cheque with their order forms -- a blank cheque, signed -- and the wholesale grocer fills in the order to the best of his ability and then fills in the amount on the cheque. We would love that in our business.

THE CHAIRMAN: But that does not happen?

MR. McKELLAR: No.

COMMISSIONER WALLS: Before going on to the various facets of the Act as it stands today, I would like to deal with your suggestion that you should be compensated to the extent of 5% of the tax collected. The first point is that in retail, sales tax, which would cover a great many more outlets and smaller outlets -- can be done on 3%. That makes 5% seem high. If you are going to pay compensation, do you not have the same justification to pay compensation to business firms for making deductions from wages for payment of income tax? Are you not creating quite a precedent for the federal government by compensating one tax collector and not compensating another?

MR. HOSKINS: Mr. Walls, this sales tax has reached the point -- not recently, but over a period of years -- at which it has become a fairly costly thing. At the moment you have a

manufacturer and a licensed wholesaler collecting a portion of your over-all taxes and they are collecting taxes which are to the benefit of the whole nation. Five per cent may be a little high -- it may be high in relation to what the provinces are paying -- but on the other hand is 5% of the tax an unreasonable figure in relation to the cost?

COMMISSIONER WALLS: At the present time this whole tax has been collected at a cost of half of 1%.

THE CHAIRMAN: Not including the cost borne by the licensees.

MR. HOSKINS: This is the government cost.

COMMISSIONER WALLS: That is right.

MR. HOSKINS: There is a lot of work in this. You have to change your catalogues twice a year and you have to have special deals.

THE CHAIRMAN: To pay 5% one would have to increase the rate by half of 1%.

MR. HOSKINS: Three per cent would be something better than nothing, but I doubt if 3% of the tax would compensate the person who had to collect the sales tax for his costs.

COMMISSIONER WALLS: In regard to the top of page 5, you say a wholesaler cannot secure a licence unless he can prove that 50% of his sales of goods for three months were exempt. Have you any idea why that was put in like that?

MR. HOSKINS: Do you mean the wording?

COMMISSIONER WALLS: No, why it was necessary in order to be licensed that he should for three months sell over half of his produce as taxable items. What caused this regulation?

MR. HOSKINS: This went back to 1937 or 1938.

MR. McKELLAR: During the depression years there were some wholesalers of some trades who were importing goods -- this is what I have understood from the Excise Tax Department -- and they would bring in just a small quantity and have it cleared and pay their sales tax, and the next month they would bring in a bigger quantity and then the next month they would bring in a great big quantity and, their credit having been established, they would fail. The government were unable to collect the sales tax so the government made restrictions, and in 1937 the Act was changed and this part was put in providing that a wholesaler had to do 50% of his business in this way and had to put up a bond.

Now what is happening is that in our membership we have approximately 10 members who have a licence and the balance have not a licence and the accounting procedure is getting very, very complicated.

COMMISSIONER WALLS: I did note that when they put this into effect in September 1938 anybody who was a registered wholesaler at that time was able to come in on the licensing. It is only since then that the 50% has been enacted.

MR. McKELLAR: Since then, yes. Before

that they did not have to do it. If they had a licence, they kept it.

COMMISSIONER WALLS: And I could not understand why it was done in the first place.

MR. McKELLAR: That is what the staff of the Excise Tax Department told me about a year ago.

COMMISSIONER WALLS: At the bottom of that page you say:

"At the present time, a manufacturer or licensed wholesaler may sell his goods at a tax included price because of the lack of enforcement of regulation 15(2). In such cases, the unlicensed wholesaler or the ultimate consumer does not know the amount of sales tax included in the amount of his purchase."

Section 15(1) states that he does not require to show the tax to the retailers and section 15(2) states that when sold to a licensed or unlicensed wholesaler the invoice must state the amount of tax separately.

MR. McKELLAR: Yes.

COMMISSIONER WALLS: What have you to back your statement that the government is not enforcing that section?

MR. HOSKINS: You hardly ever see that although it is required under the Act. It is very rarely done. You have a tax included price, and that is it.

COMMISSIONER WALLS: Is that because of the question of the two sections and where it is to a retailer you do not have to share it? Is it because many manufacturers are not clear on the taxes when they sell to another licensee that they have to share it?

MR. HOSKINS: Originally it was intended that that tax should be shown in order to disclose what the tax was, and if there were any adjustments subsequently there would be a base there for determining what it was. I suppose just through ordinary business procedures, and possibly because of the amount of work involved in one way or another, it has just gone out of the picture.

MR. McKELLAR: In the price from the manufacturer to the unlicensed wholesaler in some industries, in most cases the price is f.o.b. delivered to the city where they are, freight included. There is no tax on freight. So it is very confusing to the wholesaler who does not know how much tax he has paid or, depending on his standing in the industry, how much he can force the issue. Then he comes to the point where he sells some of his merchandise to a customer who has a permit not to pay the tax. So what does he allow him? He allows what the trade says -- 9.91, that is the competition. Then he makes a claim on the government to get his tax back and in every case he has an argument with the government -- I do not know of a case in which there has not been such an

argument -- as to how much tax he paid because he has no proof.

COMMISSIONER WALLS: Was the reason for it not being required of the retailer not so that the retailer would not know what the wholesaler's margin was in between,and that is much the same where you are dealing with government buyers. If you shared that, would you not run the danger of the larger retailer using it to his advantage and beating down your prices, and also that the government purchasing agents would do the same thing?

MR. HOSKINS: That is true. Today if you want to find out what rate you should use for tax rebate you have a pretty difficult time finding out what the manufacturer's selling price is because he does not want to disclose his profit, and probably the subsequent wholesaler does not want to disclose his profit.

MR. McKELLAR: On page 9 we have an example of one of our members who shows what he has lost because he has been unable to prove it.

COMMISSIONER WALLS: I saw that, yes. I can see the difficulty of disclosure to the retailer and, as you mentioned later on, in regard to the method of operating with government departments where you want them to apply for the rebate direct instead of the wholesaler having to work it out. Am I right in that?

MR. HOSKINS: Yes.

COMMISSIONER WALLS: If you get him having

to work it out, it is not going to take him very long with the tax at the manufacturer's level to be able to figure out what the fellow in between is getting out of it, and that gives him a marvellous weapon for negotiating for lower prices. Therefore I can see why perhaps that section is not being utilized to the extent it was.

What I would like to ask you now is this. If we go to a wholesale tax, do you believe then that in your wholesale tax you should in all accounts show your tax above the wholesale price or the tax to the retailer?

MR. HOSKINS: In other words, a tax extra?

COMMISSIONER WALLS: Yes.

MR. HOSKINS: No, we do not think the same serious problem arises because you are levying tax at the point where it is billed to the retailer or end user, and we believe there would be relatively few rebates where the tax percentage would have to be used.

Getting right down to brass tacks, I suppose they make people tax conscious and not allow a tax included selling price, but have a tax added price in every case. I do not know whether that is good business however.

COMMISSIONER WALLS: But generally speaking you believe you would rather have a hidden tax? If the sales tax is moved to the wholesale level you would rather supply the retailer

with an all-inclusive price rather than invoicing him with the cost of your article with tax extra?

MR. HOSKINS: There is another thing that might be worthy of consideration.

THE CHAIRMAN: Did you answer that question, Mr. Hoskins? Did you answer that in the affirmative?

MR. HOSKINS: As to tax on the wholesale level?

THE CHAIRMAN: Whether tax should be shown.

MR. HOSKINS: I would say from the viewpoint of our clients, a tax included price.

There is another point that might be worthy of consideration. If the tax were levied at the wholesale level and any rebates were involved, that is where a retailer happened to sell a manufacturer and another wholesaler, whether you could not arrive at a flat rate and just allow a flat rate where the percentage on either side would not be too great. I think that would simplify it.

THE CHAIRMAN: You would have to allow a flat rate by industries, I suppose.

MR. McKELLAR: By industries, yes.

MR. HOSKINS: Yes.

COMMISSIONER WALLS: You deal with the sales tax included in bad debts write-offs on page 7. You say that an unlicensed wholesaler suffers from uncollectable accounts receivable in which is included an element of sales tax. Am I not right in

saying that this also applies to licensed wholesalers and manufacturers?

MR. HOSKINS: Yes.

COMMISSIONER WALLS: I just wondered why you only mentioned unlicensed wholesalers in dealing with this.

MR. HOSKINS: I think in the last paragraph we say that in the case of licensed wholesalers they should be allowed to deduct the sales tax. The language there is probably ambiguous. In the case of licensed wholesalers, they should be allowed to deduct the tax from their monthly instalment payments.

There might be an argument there that possibly part of that tax is a bad debt write-off and is recovered through income taxes. There should be a proper charge to the government for the amount of tax and that the taxpayer would only write off the amount of the account plus the tax. That is all he would get for income tax purposes.

COMMISSIONER WALLS: Further down the page you say:

> " We suggest that for purposes of levying sales tax on imported goods into Canada the base should be the price on which sales tax is levied in Canada on goods of similar kind and quality."

But would you not still have this problem if the tax was moved forward to a wholesale level,

but maybe to a lesser degree?

MR. HOSKINS: Yes.

COMMISSIONER WALLS: You are not going to remove the problem of having to find some method of equalizing the price between the wholesale product and the domestically produced product. You are not going to dispense with that entirely?

MR. HOSKINS: Not entirely, no. The idea is to bring it up as close as one can. It will never be right, but if one can bring it up to pretty close to what tax would be levied on a Canadian produced product, the import should pay relatively the same amount of tax for like quality.

COMMISSIONER WALLS: Would you consider putting a flat amount on all imports in order to bring it to an approximate wholesale price?

MR. HOSKINS: That would be rather difficult on the whole because there would probably be a great variation between the margin of selling price in a foreign country and the price when it is imported to Canada. There may be wide variations there.

COMMISSIONER WALLS: The reason we ask that question is because there is a recommendation of a wholesale tax that does that, that imposes a flat rate on all imports to bring it up to what they feel would be the average wholesale cost, and by setting a flat rate it may create inequity but it certainly cuts down administration costs.

MR. HOSKINS: Yes.

COMMISSIONER WALLS: And certainly your movement to wholesale tax would answer the problem stated in the middle of page 8 where you say:

"If a purchaser supplies an M & P certificate to a wholesaler, such certificate should be sufficient for the wholesaler to sell tax exempt."

This is really an end use problem and would be solved by moving the tax forward to either the wholesale or retail level, would it not?

MR. McKELLAR: Yes.

THE CHAIRMAN: I might ask you to what extent you think pyramiding occurs in your business. Is it pretty obvious that there is pyramiding?

MR. HOSKINS: No. There is some pyramiding but not to a great extent because there would not be too many transactions where one goes from, let us say, the first wholesaler to a second wholesaler to a third wholesaler, and so on. There is the general application of the tax, and that is where the unlicensed wholesaler comes into the picture. He considers the tax that is in that as a cost; consequently, if he sets his selling price he has to have a profit on his cost. The proper way is that one should show one's base cost plus one's tax, and if one is doing this thing properly one would take one's mark-up on one's original cost and not on one's sales tax.

THE CHAIRMAN: You think he is making

more profit than he would if he were doing it, as you say, properly?

MR. HOSKINS: That is right, but after all you have money invested in sales tax.

THE CHAIRMAN: I thank you both very much indeed for your assistance today and for your submission to us. We will certainly fully consider what you have put before us. It will be some time before we come to complete our report, but I can assure you that this will have full consideration at such time as we are trying to reach our conclusions.

Thank you, Mr. McKellar and Mr. Hoskins.

MR. HOSKINS: Thank you very much.

THE SECRETARY: Perhaps while we are waiting I could enter into the record one exhibit I have here, a submission from the Canadian Pacific Railway which was received January 13. I would like to enter this into the record as Exhibit 333.

---EXHIBIT 333: Submission from the Canadian Pacific Railway.

THE SECRETARY: Mr. Chairman and Commissioners, the next presentation this morning is being made by the Canadian Section of the Council of Profit Sharing Industries. Mr. W. D. Welsford, who is the Secretary-Treasurer of the Canadian Section is here together with a number of his associates. He wishes to make a preliminary statement, Mr. Chairman, and will introduce his associates to you. May I enter this into the record as Exhibit 332?

---EXHIBIT 332: Submission of the Canadian Section of the Council of Profit Sharing Industries

SUBMISSION OF

CANADIAN SECTION

OF THE

COUNCIL OF PROFIT SHARING INDUSTRIES

APPEARANCES: Hon. J. M. Macdonnell

W. D. Welsford,
Vice-President and Director
William M. Mercer Ltd., Toronto

R. M. Sedgewick, Q.C.
Partner, Messrs. Miller, Thomson,
Hicks, Sedgewick, Lewis and Healy,
Barristers and Solicitors,
Toronto

David Verity,
Executive Assistant
Dominion Foundries and Steel
Company, Limited,
Hamilton

David Meynell,
Counsel and Consultant
William M. Mercer Ltd., Toronto

THE CHAIRMAN: Good morning Mr. Welsford and gentlemen. We are delighted to have you with us. We have found your brief to be very interesting and I suppose we all have some knowledge of the principles. I have attended one of the meetings before Council and I suppose we have all seen some of the literature. You have something you would like to say first, Mr. Welsford?

MR. WELSFORD: This is a basic concept that has been developing mainly in this century gradually. In the United States it has developed very

rapidly in the past ten years to the extent that as our brief points out there are now between 3500 and 4000 profit sharing plans in the United States as compared to something around 300 in Canada.

The concept is one in which a great deal of interest is being taken by an increasing number of people, all trying to find the answer to the present and general pattern between management and labour whereby at present both tend to be divided and are striving against each other, with the inevitable result that there is no full co-operation as is needed and is going to be increasingly needed in order to improve the productivity in this competitive world of ours.

At the same time to attain this co-operation to pass some of the rewards along to the employees. This is also of quite a benefit to the government so its a three-party problem.

As I say, an increasing number of people have being paying attention to this. On the one extreme there are those that propose compulsory arbitration as a solution to the problems. I must confess I find the word distasteful so that I think if its proponents were successful it would ultimately lead to some disastrous effects between management and labour.

On the other hand is the concept that is represented by this brief. As I indicated, an increasing number of people having been paying attention to this. In the United States we see that University of Wisconsin has set up a center for product-

ivity of motivation. Stamford University has set up an extra curricular course which includes profit sharing. Very recently we were pleased to see announced that York University in Toronto is going to set up a seminar, which will be held for seven years in the spring of each year, and to study this general problem.

There have been as a result a number of new phrases coined such as socio-economic sharing and productivity sharing, progress sharing and profit sharing. These are generally in the same pattern, trying to find the answer to this problem. Now, the thing that concerns us is: what can the government do? It is our feeling that the responsibility of the government is to provide an atmosphere that will encourage, not deter, profit sharing. In the United States in 1938 the Vanderbilt Senate Sub-Committee conducted a study on this aspect. As a result in 1939 profit sharing legislation was established which had the effect of encouraging profit sharing.

In Canada we have been making representations to the government for the past 10 years and have gradually been making an impression to the point in in 1961 profit sharing legislation was established. We feel that it is particularly important for the government to become involved in this, to set the proper atmosphere. One of the main reasons for the present action/is the reform legislation that you see particularly in Ontario, Ottawa,-certainly will affect all provinces. We feel that there are certain inequities in the legislation at the present

time which act as a deterrant to profit sharing and in particular I would like Mr. Bob Sedgewick of Miller, Thomson, Hicks, and Sedgewick to outline those points.

THE CHAIRMAN: Before we get to Mr. Sedgewick, would you care to introduce to us the rest of the delegation?

MR. WELSFORD: I am sorry.

THE CHAIRMAN: For my part I will introduce to you the Commissioners but their names are all before them here. I will be very glad to know more about your delegation.

MR. WELSFORD: I apologize, Mr. Chairman, On my extreme right the Hon. J.M. Macdonnell, a Member of Parliament.

MR. MACDONNELL: Once.

MR. WELSFORD: Mr. David Verity, the Executive Assistant of Dominion Foundries and Steel. On my extreme left Mr. Bob Sedgewick of Miller, Thomson, Hicks and Sedgewick and Mr. David Meynell of William M. Mercer Ltd.

THE CHAIRMAN: You are associated with that firm yourself?

MR. WELSFORD: I am.

MR. SEDGEWICK: So far as the Income Tax is concerned, Mr. Chairman, Section 79 (c) which was enacted in 1961 does the principal job which is necessary to encourage profit sharing in that it defers tax on profit sharing credit until the time of ultimate withdrawal and then imposes the tax at an

average rate set out in Section 36.

We feel, however, that there are three principal provisions that are not contained in Section 79 (c) and that would help encourage the growth of profit sharing.

The first one is that the employee's contributions to the profit sharing plan are not deductible. This is of consequence for two reasons. The first one is that it appears to be the only form of saving for retirement, which is not encouraged by means of a tax deduction or tax deferment.

In the second place, the bulk of the profit sharing plans that have been put into effect allocate the contributions which the employer makes on some basis which bears reference to the contributions by the individual employee. An indication of the interest in the plan or desire to participate is evidenced by the amount of the contribution they make up to a certain maximum level and at least, so far as the bulk of the plans are concerned the employers' contributions are allocated by reference to its employee contributions.

Thirdly, we feel that the existing limit of $1500 on the deductibility of employers' contribution, which limit must cover both pension contributions and profit sharing contributions, tends to be restrictive and may in itself prevent a proper development of the profit sharing plan.

Generally speaking profit sharing plans tend to produce larger allocations to employees

who have been in longer service and who, of course, are approaching the age of retirement. In respect of these individual employees it may well be that their participation in the employers' contribution would exceed $1500 a year even though the average for employees across the board would be substantially less than $1500 a year and we suggest for your consideration that the test of deductibility be one that is related not to the individual employees but rather to the total company payroll, leaving it to the provision of the plan to allocate that total contribution among the employees in any fashion that seems to be best for their retirement provision.

In the United States the limitation of deductibility of employers' contributions under profit sharing is 15 per cent of total payroll annually with no additional requirement that it cannot exceed the sum stated as far as each individual employee is concerned.

The very point I would like to bring to your attention is that the present provisions of 79(c) tends to discriminate against Canadian employees of either U.S. or of some foreign firm or of subsidiaries of some foreign firm because if there is a profit sharing plan in existence covering the corporate chain that the pattern, outside of Canada, the Canadian employee cannot obtain tax deferment unless the plan is broken down so as to be applicable only to Canadian employees on the one hand and the balance of the employees on the other.

Section 79(c) requires that the trustees of the plan accepted for registration must be Canadian residents and it goes further to say that 90 per cent of the investments must be Canadian securities. We recognize that in addition to the tax deferment and registration of foreign plans, the problem of tax collection at the time of retirement may exist. We suggest that means of handling that problem could be found other than the rather restricted requirement which is now in the Act which says you must start your plan down and have an individual plan for the benefit of your Canadian employees.

That, in a summary way, sets out the three additional provisions which, as I say, we would like to see included in Section 79(c).

THE CHAIRMAN: The significant word in this thing, of course, is "deferred". Anyone can divide up profits, but that represents no problem at all. It is the question of deferring benefits to some other time when you release them.

Does Section 79 provide a useful purpose in the Act or has that ceased to be significant now that we have Section 79(c)?

MR. WELSFORD: I think generally it ceases to be a significant factor in the Act with the exception of providing legislation for foreign profit sharing plans and for thrift plans.

THE CHAIRMAN: Thrift plans?

MR. WELSFORD: Thrift plans are a class of plan whereby the employee contributes 50 cents

or rather for each one dollar the employee contributes, the company contributes 50 cents. This is the type of plan that is predominant in the oil industry and has branched out in a relatively small section of other industry.

THE CHAIRMAN: Would the reason that there are limits imposed on the extent of the deferment be because of the thought that it should be kept in line with the pension restriction?

MR. WELSFORD: Yes, that is correct. I think we feel the same way about the restriction on pension plans.

THE CHAIRMAN: You feel that the limit of $1500, which is the same for pensions, is not realistic?

MR. WELSFORD: No, I agree I don't think it is realistic. In the case of pension plans, there are other means such as by the use of Section 76 whereby you could distribute larger amounts to individuals which is not available under a profit sharing plan.

THE CHAIRMAN: Under the profit sharing plans, there must be many instances where the amount exceeded $1500 right now?

MR. WELSFORD: Yes.

THE CHAIRMAN: There are many successful profit sharing plans where the amount for distribution amounts to $2000 or $2500. Is the $1500 amount deferred and the balance paid out right away?

MR. WELSFORD: Yes. In the majority

of cases the maximum distribution under the deferred profit sharing plan is limited to $1500 and the balance paid out in various ways. It can be transferred into the pension plan as an employee contribution.

THE CHAIRMAN: Which is not permitted as a deduction?

MR. WELSFORD: Under our pension plan, no.

COMMISSIONER PERRY: I was interested in Mr. Sedgewick's statement that the employer contribution is normally allocated by reference to the employee contribution. What do you do with a plan when there is no employee contribution? Does this mean that there has to be an employee contribution in all plans?

MR. SEDGEWICK: No, it doesn't mean that there has to be. In quite a number of plans there is no employee contribution.

COMMISSIONER PERRY: What is your basis for allocation then?

MR. SEDGEWICK: One of several bases may be used; salary, length of service, distribution can be equalled, for example, ---

COMMISSIONER PERRY: To suit the employee?

MR. SEDGEWICK: Yes. In addition to these plans where there is employee contribution I think I am correct in saying that the bulk of the employer allocations are made by reference to that contribution.

One of the items that this permits is weighing the allocation of the employers' contribution in favour of longer service employees as, for example, you can compute the employers' contribution times one if he had been there five years or else times two if he had been there five to fifteen years or times three if he had been there fifteen to twenty-five years or any other multiple you may work out which tends to allocate the larger amount to the employee as he gets closer and closer to retirement.

COMMISSIONER PERRY: What proportion of the existing plans in fact do have an employee contribution?

MR. WELSFORD: It is probably close to two-thirds or three-quarters. It is a very substantial percentage.

COMMISSIONER PERRY: Even with the present tax discouragement?

MR. WELSFORD: The majority of the deferred profit sharing plans in Canada are registered pension plans.

COMMISSIOER PERRY: So in effect they are pension plans with variable employer contributions?

MR. WELSFORD: That is correct.

THE CHAIRMAN: They do not come under Section 79(c).

MR. WELSFORD: No, a number of them will undoubtedly wish to change to the pension plan, 79(c) with the introduction of the Ontario legislation proposal.

THE CHAIRMAN: Why?

MR. WELSFORD: Because the Ontario legislation imposes certain restrictions on pension plans which in other ways are not connected with profit sharing such as lump sum distribution at retirement and distribution before retirement.

THE CHAIRMAN: Would there be many plans under 79(c) now?

MR. WELSFORD: I think our best estimate is around 40.

MR. SEDGEWICK: I thought it was more than that. Mind you, the figure is misleading because in addition to the single plan covering employees in the usual way or 10 companies in a corporate group, they require individual legislation for each of the 10 companies despite the fact only one plan is operating so the legislation figures tend to be misleading. I was under the impression there were more than 40.

THE CHAIRMAN: The Minister has established a certain criteria to permit legislation. Do you find that difficult to meet?

MR. WELSFORD: No sir. There has not been any difficulty in any of the standard plans that have been established in the past two or three years.

THE CHAIRMAN: He has not printed that criteria. I understand that there are a number of tests to which this is subjected before he grants his permission.

MR. WELSFORD: Yes. We have received a letter from the Department which sets out their

criteria.

THE CHAIRMAN: Have you?

MR. WELSFORD: Yes.

COMMISSIONER PERRY: What are the considerations that the government set whether you apply under 79(c) or are registered as a pension plan?

MR. WELSFORD: One of the considerations is lump sum distributions at retirement. One is the ability to invest in your own common stock, which is restricted under the Ontario legislation. I think those were the two principal ones.

MR. VERITY: The taxation status of the employee, of course, is one of the major considerations when determining between a profit sharing plan and pension plan registration.

One of the very difficult impositions when making this decision and when profit-sharing amounts and employee savings are significant is the source of the funds to pay the tax on an amount which has been deferred until retirement.

There is a net reduction in employees' available funds, take-home funds, in order to pay the tax when profit-sharing amounts are tax free at pay-out.

COMMISSIONER GRANT: Mr. Sedgewick, your suggestion is that the amount that the company be permitted to contribute would be determined on the basis of this total payroll?

MR. SEDGEWICK: Or some similar plan that does not relate to amount to each individual employee.

COMMISSIONER GRANT: And I also think it has been said that the deferred plan has application largely to owner-employees.

MR. SEDGEWICK: Yes, and older employees rather than more recent employees.

COMMISSIONER GRANT: So when the payroll is made up of younger employees their contribution to the plan would really be lending the amount which they take as wages as a percentage of the allotment to the plan?

MR. SEDGEWICK: Yes.

COMMISSIONER GRANT: As I understand page 13 of the brief, there is an employer tax liability

on the pay-out. Is that fair?

MR. SEDGEWICK: No.

COMMISSIONER GRANT: "... tax liability on the employer contribution is incurred only when the proceeds of the account are actually received by the employee or his beneficiary." Does that mean received under the plan or actually received when the employee terminates his employment?

MR. SEDGEWICK: I am sorry, I misunderstood your first question. It is taxed in the employee's hands only at the time it is actually paid out to him. The employer at that stage is not involved, of course.

COMMISSIONER GRANT: So there is a tax liability there on the part of the employer?

MR. SEDGEWICK: On the part of the employee.

MR. WELLSFORD: This is primarily American tax law.

COMMISSIONER GRANT: The section I am reading from has no application to Canada?

MR. WELLSFORD: No.

MR. MEYNELL: The last pararaph on page 13 and the top two paragraphs on page 14 are American law.

COMMISSIONER BEAUVAIS: The employer is not taxed on the whole amount? When he pays his contribution, that is not deductible?

MR. WELLSFORD: No.

THE CHAIRMAN: Just the part paid by the employer is subject to tax?

MR. WELLSFORD: That is correct, and the income of the fund.

COMMISSIONER PERRY: Does it qualify for the three-year alleviation that applies to lump sum pension payments?

MR. WELLSFORD: Yes.

MR. SEDGEWICK: If it is a total withdrawal and it corresponds to the termination of employment.

THE CHAIRMAN: I must say I am appalled at the idea which I take it you would like to see of an employer being able to invest the funds for his employees' old age in his own enterprise and put them at the risk of his own business. That does not appeal to me very much.

MR. WELLSFORD: It is held, of course, in a trust fund which is held for the benefit of the employees. I would say not more than 30% of the deferred plans would invest in the employer common stock,and then only to a limited percentage.

Probably one of the most successful profit-sharing plans in the world is Sears Roebuck.

THE CHAIRMAN: Which is all in the company's stock.

MR. WELLSFORD: A very high percentage. In fact, the Sears Roebuck fund controls 25% of the stock of Sears Roebuck and has been tremendously successful.

THE CHAIRMAN: Of course, the plan is predicated on that and when the employee participates in the plan he recognizes that his share of the profits is going to be invested in the company, and that is fair enough I think.

COMMISSIONER PERRY: What is happening in the pension plans now? Investments in companies' owner shares used to be discouraged, but is it developing now?

MR. WELLSFORD: Of course, as you know, the regulations have been --

COMMISSIONER PERRY: Obscured?

MR. WELLSFORD: Virtually wiped out. But as a general rule in pension plans the employees do not invest in common stock. Basically the purpose of that fund is to provide life annuities to the individuals and a greater degree of security is provided.

THE CHAIRMAN: There is no law that restricts them in the case of pension plans?

MR. WELLSFORD: Not at the present time, but there will be when the Ontario plan comes in.

MR. MEYNELL: We have seen evidence when inquiries are made in respect of investment, they like to see an earnings record to show that the stock is a good investment.

COMMISSIONER PERRY: Is the American treatment on all fours with ours regarding employee

contribution? Generally they are pretty niggardly about deductions for employees.

MR. WELLSFORD: They do not permit deductions.

COMMISSIONER PERRY: There is no deduction there.

COMMISSIONER GRANT: There is a reference to the annuity in the middle of page 14 where you begin by saying:

"Another major advantage occurs when the employee elects to have the fund buy an annuity for him."

This again has reference to the United States, has it?

In that case the annuity is subject to tax, not the interest portion?

MR. WELLSFORD: No, under Section 29(c) it is permissive to purchase an annuity at retirement, in which case the employee's contribution or that portion representing the employee's contribution would be exempt; the portion representing the employer's contribution and the income would be taxable.

COMMISSIONER GRANT: In this deferred plan is there any philosophy that states that the employer's contribution itself includes the employee's contribution because he has contributed to the profits?

MR. WELLSFORD: There is a philosophy that one of the purposes of a deferred profit-sharing plan is for retirement security. Therefore it is of advantage to have employee contribution to further increase his retirement security. I would not say that it is an integral part of the philosophy but, as I mentioned, about two-thirds or three-quarters of the plans do have employee contributions.

MR. VERITY: If I may supplement your comments, Mr. Wellsford, in this regard of employee savings I think there are several aspects here to be considered, and one is when profit-sharing plans were first initiated they were rarely taking account of past services, as is done in pension plans. Therefore there is something of a problem to build up adequate values to the credit of individual employees in the initial years. The employee contribution helps do this. During those initial years when selling the concept of profit-sharing is most important with the employees, the saving part becomes an integral feature of the plan and makes the employee much more conscious of his own contribution toward the company's profits. I think in established plans the employee saving is much less significant because usually in long term established plans the total credits are such that the plan could be successful and maintained on company contributions alone.

THE CHAIRMAN: The employee contributions being placed on all fours with what is permitted under

ordinary pension plans?

MR. VERITY: I did not quite understand the question.

THE CHAIRMAN: Could employee contributions be limited in such a way as to make them comparable or to put them on all fours with employees' contributions under an ordinary pension plan?

MR. VERITY: Yes.

MR. WELLSFORD: Yes, that would be highly acceptable.

COMMISSIONER PERRY: I would like to ask about the people who contribute to or are members of foreign profit-sharing plans. This gets a little sticky, does it not, when you have an American who has come up here and lived here for a while and is going to go back to the States? Are they not likely to give him a tax deduction while he is here on the assumption that some time later on you are going to tax the pay-out and he will lose out on that? The amounts here are not very large, but there is a principle.

MR. SEDGEWICK: We recognize that as a problem. We suggested at one stage that if foreign plans could be registered here without the necessity of establishing a separate Canadian plan, it would be possible for the plan to appoint an agent, shall we say in Canada who was responsible for the collection and withholding of the tax that had been deferred either at the time of retirement or at the time of

departure from Canada, more or less the same type of withholding agent as is now provided for in section 110 in relation to real estate income from Canada.

THE CHAIRMAN: Why not impose on it the need for establishing a Canadian plan, which in fact is what the situation is at the present time? Does it add to the cost materially or does it cause great difficulties which should not result?

MR. SEDGEWICK: It distinguishes between employees in the same corporate group to start with, and it prevents the Canadian employee from participating in the more rapid growth of an already established and well functioning plan. It forces you to start from scratch at that particular stage where investment in shares of a company, for example, is not permitted or is permitted only to the extent of 10% of the investments. Generally speaking, he does not get the same opportunity of growth or accumulation in his account as he would if he were a member of the more general plan applicable to all employees.

THE CHAIRMAN: Perhaps there is something in those arguments, although if you start from a small base your opportunity for growth is greater than starting from a larger base. Secondly, as far as composition of the investments goes, if Canadian laws are restrictive I would have thought that we should impose the Canadian laws on participants in a plan in Canada.

MR. SEDGEWICK: Mind you, this question

is also affected by the industry. In the oil industry where the Canadian companies with their Canadian employees are essentially in the exploration end, the Canadian company that employs the Canadian participants would not of course have any income annually out of which to make a contribution to a profit-sharing plan, whereas on a more consolidated basis, taking into account world-wide operations, there would be a substantial element. You cannot say that, of course, in reference to all consolidated plans of foreign countries, but there are glaring examples, particularly in the oil field.

COMMISSIONER PERRY: What do you do on a branch operation? Do you set up a plan which would similarly be based on the profits of the branch?

MR. SEDGEWICK: Branch operation of a foreign company?

COMMISSIONER PERRY: Yes.

MR. SEDGEWICK: Yes, that is the only alternative.

THE CHAIRMAN: Well, that is the same difficulty we have with regard to pensions, is it not?

MR. SEDGEWICK: Yes.

THE CHAIRMAN: Or relatively the same.

MR. SEDGEWICK: Yes.

MR. WELLSFORD: Although in pensions we have had a variable employer contribution. You can vary distribution of Canadian employees on

consolidated profits.

THE CHAIRMAN: Can you? You can take into consideration foreign profits.

MR. WELLSFORD: Yes.

THE CHAIRMAN: Yes, but you take them in not to the same extent as one would be taking them in under a profit-sharing plan.

MR. WELLSFORD: No, I think you could take them in to the same extent.

THE CHAIRMAN: Do you?

MR. WELLSFORD: Yes.

THE CHAIRMAN: Could you give us some reference as to where we find that or some material? Could you write us a letter, perhaps?

MR. WELLSFORD: I will write a letter.

THE CHAIRMAN: I wish you would. That surprises me a little because I did not fully understand it -- and I do not now, but if you wrote a letter I think I would.

COMMISSIONER PERRY: This sort of thing does not very often get down in writing.

MR. WELLSFORD: Well, it gets approved.

COMMISSIONER PERRY: This whole area is now very vague. There is certainly not much law on it and certainly not much administrative regulation or ruling on it.

MR. WELLSFORD: No. I think where you get around the vagueness is that you can base the distribution -- or to Canadian employees you can base the consolidated profits, but the percentage

distribution to Canadian employees can vary from that of the parent company as long as you stay within your limit of, say, $1,500. It is not necessary in a deferred profit-sharing plan to set up a specific formula to which you must rigidly stick. You can have a variable formula.

THE CHAIRMAN: Can you change the formula as you go along?

MR. WELLSFORD: Yes.

THE CHAIRMAN: I think we have run out of questions, gentlemen. I think we understand, as far as we are capable of understanding what you have put before us. To the extent we are not immediately capable of understanding it, we will try; that is all I can say. We will keep on examining it. This is an important area and I agree this is a very important submission. Certainly we would not like Canadian laws to frustrate the benefits which you indicate ought to be derived from profit sharing.

Thank you very much indeed for putting this before us and coming to see us today; it is very good of you.

MR. WELLSFORD: Thank you very much.

THE CHAIRMAN: The hearing will stand over until 9:30 tomorrow.